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STRATEGIC MARKET PERSPECTIVE

Identifying & Winning Outsourcing Opportunities

Europe, 1994

Outsourcing Programme—Europe

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Identifying & Winning Outsourcing Opportunities – Europe, 1994

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Abstract

Outsourcing is now well-established in Europe. Nonetheless, vendors still find it difficult to identify prospects for outsourcing in advance of the prospective client issuing requests for information. In addition, it can be difficult for vendors to forecast the outcome of bids. Frequently, a number of vendors appear to be offering very comparable combinations of service and price.

The purpose of this report is to assist vendors in identifying outsourcing prospects by analysing the circumstances under which organisations tend to adopt outsourcing and the key triggers that determine the timing of the decision. In addition, the report analyses the key factors that are used to analyse vendor suitability and addresses the specific criteria that prospective clients typically use to differentiate between vendors when making their final choice of vendor.

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Table of Contents

I	Introduction	I-1
	A. Scope and Objectives	I-1
	B. Methodology	I-6
	C. Report Structure	I-7
	D. Related Reports	I-7
II	Executive Overview	II-1
	A. CFO's Initiate the IT Directors Select	II-1
	B. CFOs Evaluate Outsourcing to Facilitate a Change of Architecture	II-3
	C. Sensitivity to Client Needs is Critical	II-5
III	Need For New Systems Causes CFOs To Investigate Outsourcing	III-1
	A. Chief Financial Officers Initiate IS Outsourcing	III-1
	B. Outsourcing Occurs Against a Background of Skill Shortages	III-6
	C. Outsourcing is Triggered by a Major Systems Development Need	III-10
	D. CFO's Perceive Low Value For Money from IT Departments Subject to Outsourcing	III-16

IV	IT Directors Favour Vendors Offering Flexible Outsourcing Contracts	IV-1
	A. IT Directors are the Key Parties in Vendor Selection	IV-1
	B. Contract Flexibility is Important in Final Stages of Vendor Selection	IV-4

A	User Questionnaire	A-1
	A. Initiation	A-1
	B. Vendor Selection Criteria	A-4

List of Exhibits

I	-1	Business Operations Outsourcing	I-4
	-2	Information Systems (IS) Outsourcing Service Categories	I-4
	-3	Outsourcing Service Components	I-5
	-4	Interview Profile by Country	I-6
	-5	Interview Profile by Respondent Type	I-7
II	-1	Outsourcing Buying Process	II-1
	-2	Key Motivations for Outsourcing	II-3
	-3	Principal Outsourcing Triggers	II-4
	-4	Key Evaluation Criteria	II-6
	-5	Key Criteria Influencing Bid Outcome	II-7
III	-1	Principal Initiators of Outsourcing Europe	III-1
	-2	Principal Initiators of IS Outsourcing France	III-3
	-3	Principal Initiators of IS Outsourcing Germany	III-3
	-4	Principal Initiators of IS Outsourcing UK	III-4
	-5	Principal Initiators of Outsourcing by Respondent Type	III-5
	-6	Background to IS Outsourcing Europe	III-6
	-7	Background to IS Outsourcing France	III-7
	-8	Background to IS Outsourcing Germany	III-8
	-9	Background to IS Outsourcing UK	III-8
	-10	Reasons for IS Outsourcing by Respondent Type	III-9
	-11	Extent to Which Outsourcing was Triggered by a Specific Event	III-10
	-12	Extent to Which Outsourcing was Triggered by a Specific Event	III-11
	-13	Triggers for Outsourcing Europe	III-12
	-14	Principal Triggers for Outsourcing France	III-13

-15	Principal Triggers for Outsourcing Germany	III-14
-16	Principal Triggers for Outsourcing UK	III-14
-17	Triggers for Outsourcing by Respondent Type	III-15
-18	IT Efficiency and Effectiveness Prior to Outsourcing	III-16
-19	Perceived IT Efficiency and Effectiveness Prior to Outsourcing	III-17
-20	Perceived Strength of Relationship Between IT Management	III-18
-21	Reporting Relationship of IT Director	III-19

IV

-1	Decision Makers: Vendor Selection	IV-1
-2	Vendor Evaluation Criteria Europe	IV-3
-3	Reasons For Selection of Successful Vendor	IV-4
-4	Criteria Influencing Final Choice of Vendor Europe	IV-6
-5	Key Criteria Influencing Final Choice of Vendor France	IV-7
-6	Key Criteria Influencing Final Choice of Vendor Germany	IV-7
-7	Key Criteria Influencing Final Choice of Vendor UK	IV-8
-8	Key Selection Criteria by Respondent Typ	IV-8
-9	Perceived Role of Outsourcing Europe	IV-10
-10	Reasons for Vendor Rejection	IV-11
-11	Level of Satisfaction with IS Outsourcing	IV-12



Introduction

A

Scope and Objectives

Outsourcing has become well-established in Europe in recent years. Nonetheless, the majority of outsourcing contracts are won by vendors responding to requests for tenders or information from organisations. Vendors typically still find it difficult to predict which organisations are likely to adopt outsourcing and which are not. In addition, it is often difficult for vendors to identify why a particular supplier has been awarded the contract. Frequently, there appears to be little differentiation between competing vendors in terms of their capabilities and service offerings.

This report aims to begin to address these issues by:

- identifying the key driving forces that lead companies to adopt IS outsourcing
- identifying any key triggers that determine the timing of the decision to adopt IS outsourcing
- analysing the relationship between the performance of the in-house IT department and outsourcing
- identifying the principal criteria used in vendor selection
- identifying those criteria that lead to successful bids and those that are characteristic of failed bids.

Outsourcing is defined by INPUT as follows.

Outsourcing is a long-term relationship (greater than one year) between client and vendor in which the client delegates all, or a major portion, of an operation or function to the vendor. The operation or function may be solely Information Systems Outsourcing-based, or merely include

Information Systems Outsourcing as an important component of the operation (at least 30% of the budget).

The critical components defining an outsourcing service are:

- Delegating an identifiable area of the operation to a vendor.
- Single vendor responsibility for performing that delegated function.
- Intended, long-term relationship between client and vendor.
- Contract term of at least one year.
- Client not intending to perform this function with internal resources.
- The contract may include non-Information Systems Outsourcing activities, but Information Systems Outsourcing must be an integral part of the contract.
- Outsourcing is a collection of services integrated under a single, long-term contract with one vendor responsible for its operation and management.

Business Operations Outsourcing (also known as Business Outsourcing or Functional Outsourcing) is a relationship in which one vendor is responsible for performing an entire business/operations function including the Information Systems Outsourcing that supports it. The Information Systems Outsourcing content of such a contract must be at least 30% of the total annual expenditure in order for INPUT to include it in the Business Operations Outsourcing market.

Information Systems (IS) Outsourcing can be viewed as a component of the Business Operations Outsourcing market (i.e., Information Systems Outsourcing is a business/operations function, see Exhibit I-1). However, in order to distinguish between outsourcing contracts that are solely IS and those that include IS as well as other functions, IS Outsourcing will be segregated from Business Operations Outsourcing. Information Systems Outsourcing is divided into four service components as shown in Exhibit I-2.

- *Systems Operations* outsourcing describes a relationship in which a vendor is responsible for managing and operating a client's "computer system"/data centre (*Platform Systems Operations*) or developing and/or maintaining a client's application as well as performing Platform Operations for those applications (*Applications Systems Operations*).
- *Desktop Services* is a relationship in which a vendor assumes responsibility for the deployment, maintenance and connectivity of personal computers, workstations, client/server and LAN systems in the client organisation. To be considered as Desktop Services Outsourcing, a contract must include a significant number of the individual services listed below:
 - Software Product Supply
 - Equipment Supply
 - Equipment/Software Installation
 - Equipment Maintenance
 - LAN Installation and Expansion
 - LAN Management
 - Network Interface Management
 - Client/Server Support
 - Logistics Management
 - User Support
 - Help Desk Functions
 - User Training and Education
- *Network Management* outsourcing is a relationship in which a vendor assumes full responsibility for operating and managing the client's data telecommunications systems. This may also include the voice, image and video telecommunications components.
- *Application Management* is a relationship in which the vendor has full responsibility for developing and maintaining all of the application or function.

Exhibit I-1

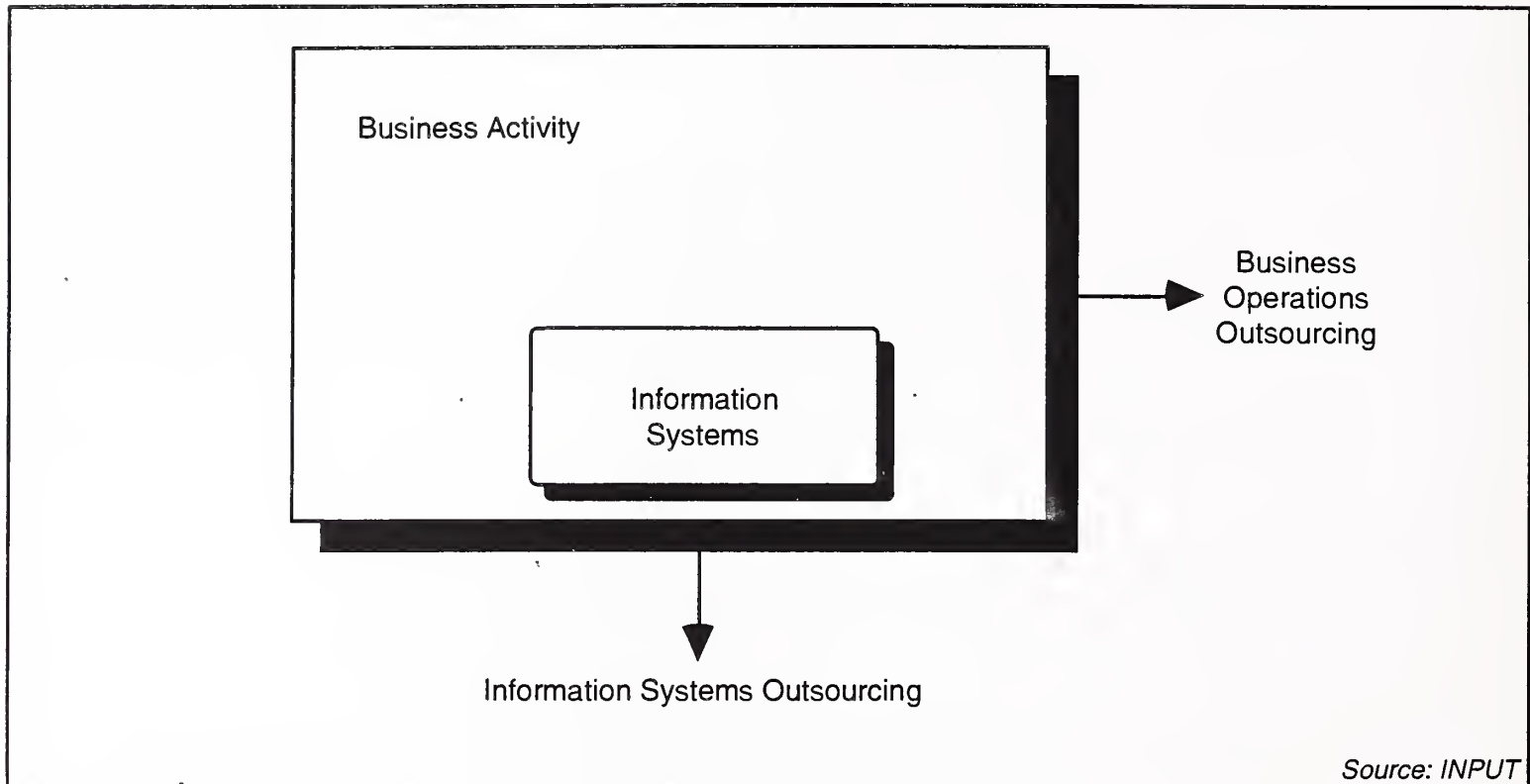
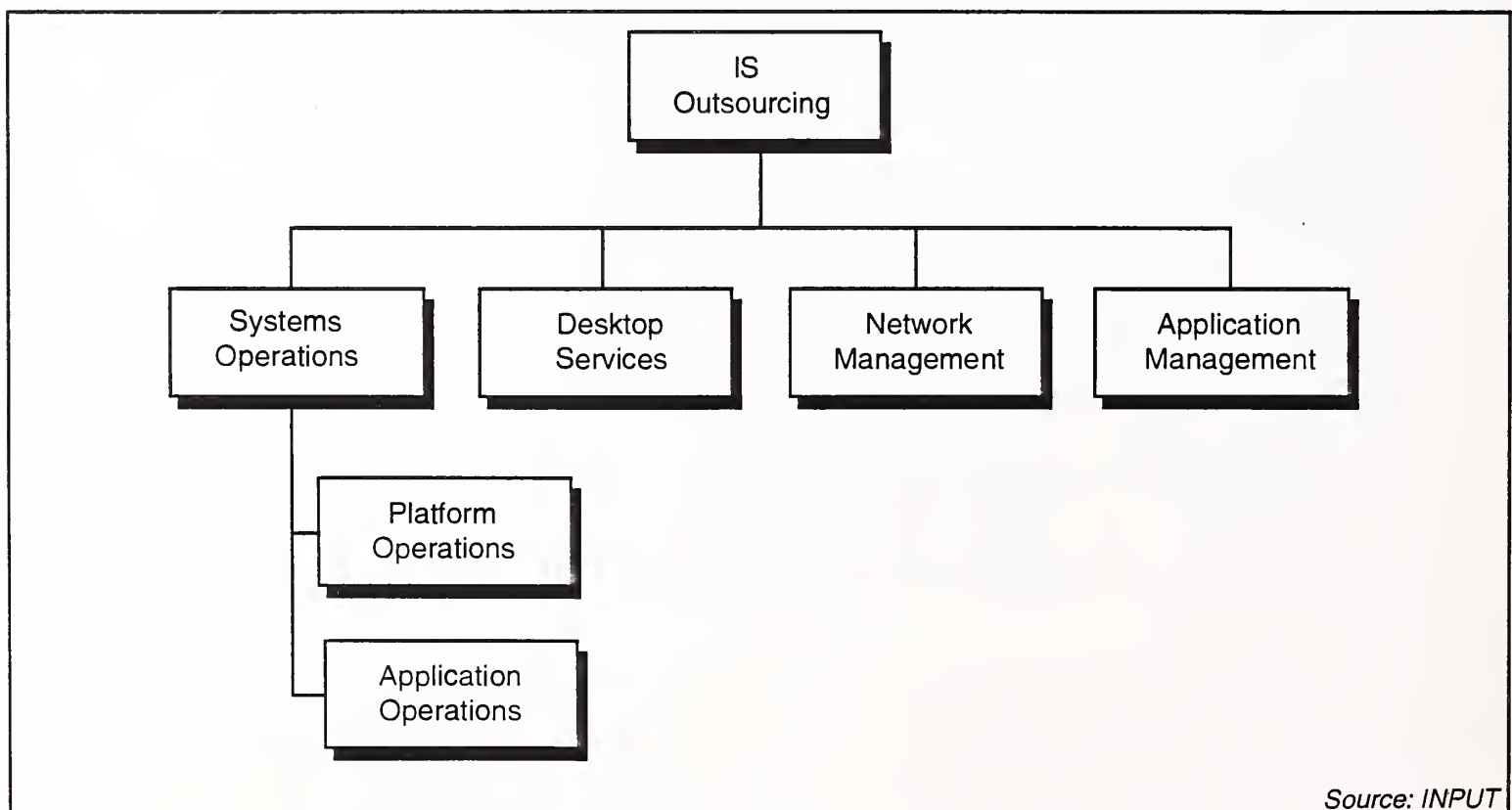
Business Operations Outsourcing

Exhibit I-2

Information Systems (IS) Outsourcing Service Categories

The above definitions focus on the services covered in the outsourcing contract. For example, an Application Operations contract can include all facets of Information Systems Outsourcing (platform operations, desktop services, network and application management). The key to INPUT's market definition is the service contract. A customer may only want to outsource network management outsourcing. If an airline, for example, wishes to outsource its reservations operation, including not only the network but also its infrastructure, applications and the people running the operation, this is a Business Operations Outsourcing contract. Exhibit I-3 shows the service components that may be included in each outsourcing service category.

Exhibit I-3

Outsourcing Service Components

Component	Platform Ops	Appl. Ops.	Desktop Services	Network Mgt.	Appl. Mgt.	Business Ops.
Project/Contract Management	X	X	X	X	X	X
Data Centre Management	X	X				X
Client\Server Operations	X	X	X			X
Equipment Maintenance	X	X	X			X
System Software Maintenance	X	X	X	X		X
Application Software Maintenance		X	X		X	X
Application Development		X			X	X
LAN Management		X	X	X		X
WAN/MAN Management		X		X		X
Transaction Processing Services		X				X
Other Professional Services		X	X		X	X
Business Process Operations						X

Source: INPUT

The largest, most visible contracts awarded over the past year have been typically Application Operation Outsourcing contracts since they, at least, included management of the infrastructure (data centres and various

computing platforms) and the support of some the legacy applications. In the past, most Application and Platform Operation Outsourcing contracts included network management but recent contracts have also included desktop services.

The following are not included in INPUT's world of outsourcing:

- Project-based services are not considered as part of outsourcing. Thus, Systems Integration and application development projects are not included.
- Services that were never intended to be performed internally. Maintenance-only services do not constitute an outsourcing function by themselves. However, responsibility for hardware and software maintenance is inherent in most outsourcing contracts.
- Processing services contracts of less than one year.
- Voice-only network management.
- Business operations with minimal information systems content. The outsourcing of the marketing communication function to an outside agency is not covered by INPUT's analysis. A function or business operation must have at least 30% of its budget attributed to information technology in order for it to be included.

B

Methodology

This report is based on interviews with representatives of 55 organisations that have already adopted IS outsourcing. The interviews were spread across organisations in France, Germany and the UK, as shown in Exhibit I-4.

Exhibit I-4

Interview Profile by Country

Country	Number of Interview
France	16
Germany	10
UK	29
Total	55

Source: INPUT

Exhibit I-5 provides a breakdown of respondents by job title.

Exhibit I-5

Interview Profile by Respondent Type

Respondent Type	Number of Interview
IT directors/managers	21
Chief financial officers	12
Other senior executives	22
Total	55

*Source: INPUT***C****Report Structure**

Chapter II consists of the Executive Overview which is a summary of the key data in the report.

Chapter III analyses the circumstances that typically cause organisations to adopt IS outsourcing. It evaluates:

- The main players responsible for initiating outsourcing within their organisations
- The factors that lead organisations to consider outsourcing
- The specific triggers that determine the timing of the decision to outsource

Chapter IV analyses the vendor selection process. It evaluates:

- The key players responsible for the evaluation of potential suppliers
- The principal vendor selection criteria used
- The key factors in determining vendor success and failure.

D

Related Reports

Outsourcing Opportunities in Government—Europe, 1993-1998

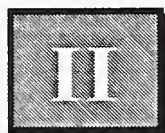
Client Satisfaction with IT Outsourcing Services—Europe, 1993

Business Operations Outsourcing—Europe, 1993

Desktop Services Outsourcing—Europe, 1994

Information Systems Outsourcing Market—Europe, 1994-1999

Impact of Business Reengineering on Outsourcing—Europe, 1994



Executive Overview

A

CFO's Initiate, the IT Directors Select

It is often assumed that an outsourcing vendor is appointed by the chief executive officer (CEO) and chief financial officer (CFO) behind closed doors. Indeed, there have been instances of outsourcing contracts where members of the in-house IT department have only received notice of their transfer to a vendor once the decision has been finalised between senior executives and the outsourcing vendor.

However, this is not regarded as good practice by the majority of vendors. The role of the chief executive officer in both initiating outsourcing and in vendor selection can easily be over-estimated. The key parties at each of these stages are indicated in Exhibit II-1.

Exhibit II-1

Outsourcing Buying Process

Role	Ranking For Each Stage	
	Initiation	Vendor Selection
Chief Financial Officer	1	2
IT Director/Manager	2=	1
Chief Executive Officer	2=	3

Source: INPUT

It is evident that CEOs are not typically the most important figures in either instigating outsourcing within their organisations or in the selection of the outsourcing vendor. CFOs are overwhelmingly perceived to be the most important parties in initiating the investigation and adoption of IS outsourcing.

However this is not because IT departments still tend to report to their CFO. In this study, the majority of IT department heads were found to report either to the CEO or the company board. Nonetheless, CFOs still appear to be more closely involved than their fellow directors, including the CEO, with the activities of the IT department.

Overall, solicitation by an outsourcing vendor was found to have been a major factor leading to outsourcing in only a small minority of cases. This does not necessarily mean that vendor solicitation is a waste of time and effort. Potential clients will tend to favour organisations of whom they have some knowledge and experience.

In the private sector, organisations tend to invite named vendors to assist their investigation into the relevance of outsourcing to their organisation and to tender for any outsourcing contracts arising from these discussions. Obviously, vendors that have existing relationships with the potential client and have already demonstrated a strong outsourcing capability are at a significant advantage relative to the competition. In extreme cases, this can lead to single-vendor tendering.

This situation also has parallels within the public sector. Although public sector organisations are required to publicise their requirements in the *European Journal*, such advertising can produce a large number of expressions of interest that can be difficult for the client to screen. Any organisation that relies solely on responding to announcements in the *European Journal* is going to have a limited success rate. For example, commenting on the current market testing programme, a representative of the CCTA remarked that any organisation that had not formed a relationship with the prospective client prior to announcement in the *European Journal* should expect to be unsuccessful in its bid.

Clearly, it is desirable for a vendor to have established its reputation with the prospective client at an early stage in the bid cycle. However, it remains very difficult for vendors to identify in advance those organisations that will adopt outsourcing in the near future.

Two possible misconceptions are that outsourcing is primarily triggered by the need for IT cost reduction and that price is the principal determinant of success. The results of this study suggest that:

- CFOs typically initiate the adoption of outsourcing to facilitate a change in IT architecture
- Sensitivity to the client's needs is a major determinant of vendor bid success

B**CFOs Evaluate Outsourcing to Facilitate a Change of Architecture**

Exhibit II-2 lists the key motivations for adoption of outsourcing as perceived by each of the main parties to outsourcing decisions. The numbers indicate the percentage of respondents that perceived this factor to be important in promoting the use or evaluation of outsourcing within their organisations.

Exhibit II-2

**Key Motivations for Outsourcing
By Respondent Type**

Reason for Evaluating Outsourcing	Chief Financial Officer	IT Directors/Managers	Other Senior Executives
Skill/resource shortfall	60	50	30
Desire to reduce IT expenditure	40	40	50
Desire to improve focus of IT department	25	45	40
Change of IT infrastructure	50	25	45

Source: INPUT

The factors are listed above in order of their relative importance across the interview sample. However, if the factors are weighted to allow for the dominance of the CFO in the decision to initiate outsourcing, then the ranking of these factors, in order of importance, becomes:

- skill/resource shortfall
- change of IT infrastructure
- desire to reduce IT expenditure
- improve focus of IT department

Accordingly, the principal motivation for outsourcing becomes not cost reduction but the lack of skill and/or resources within the in-house IT department to develop the new systems required by the organisation within a modern architectural framework. Many senior executives are impatient with the speed at which their in-house IT departments are adopting more decentralised architectures such as the client/server model. Centralised mainframe-based systems are typically regarded as

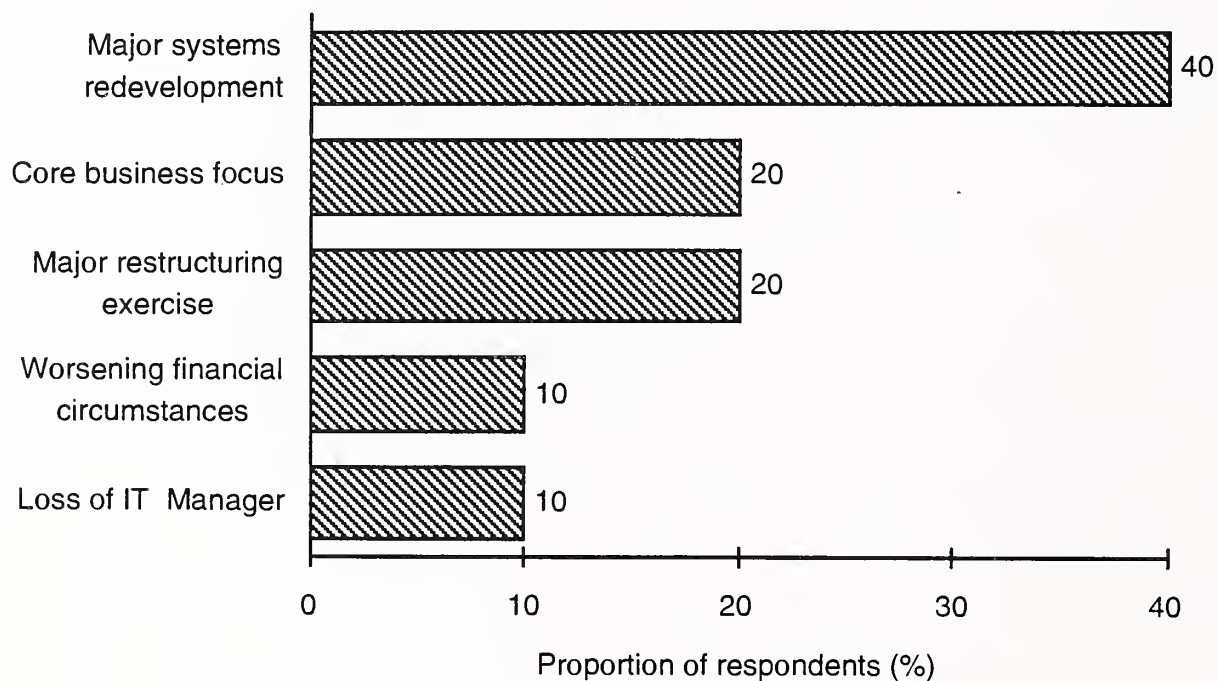
being too inflexible to react to the business needs of the organisation. However, CEOs and other non-financial senior executives, rather than CFOs, tend to view the problem primarily as one of improving the value-for-money they have obtained from their use of IT. Accordingly, the CEO may be more receptive to suggestions of inefficiency than the CFO.

It could still be argued that the precise timing of the decision to use outsourcing could be dictated by a decline in the organisation's financial position, leading to a major cost-cutting review. Clearly, there are examples of outsourcing contracts, such as British Aerospace, where financial considerations appear to have been paramount.

Exhibit II-3 lists the key factors that determined the timing of the decision to outsource. The numbers indicate the percentage of respondents that perceived this factor to be important in triggering the use or evaluation of outsourcing within their organisations.

Exhibit II-3

Principal Outsourcing Triggers



Standard error = 6%

Sample of 55 respondents

Source: INPUT

The overwhelming factor is not worsening financial circumstances but the need for major systems development. Indeed, if these factors are weighted in line with the relative importance of the respondent in the decision to outsource, then their relative ranking in order of importance becomes:

- Major systems development
- Loss of IT manager
- Major restructuring exercise
- Core business focus
- Worsening financial circumstances

Accordingly, outsourcing is not primarily a means of getting an unimportant activity off the agenda. It is often at times when IT is becoming more important to the organisation that outsourcing is adopted. At these stages, there is often a need to change the IT architecture and develop a new generation of key systems. In-house staff frequently lack the skills, and certainly the resources, to cope with these peaks of activity. Indeed, many senior executives view outsourcing as a means of protecting their organisations in the future from an over dependence on a small number of key in-house IT personnel.

Organisational restructuring is another major trigger for the adoption of outsourcing. If business units are being acquired, or disposed off, then they may move outside the scope of their existing service provider and so seek a new supplier. In addition, a restructuring may result in major changes in organisational focus or business process reengineering, producing corresponding changes in the type of information systems required.

C

Sensitivity to Client Needs is Critical

Exhibit II-4 lists the key parameters on which outsourcing vendors are judged.

Exhibit II-4

Key Evaluation Criteria

Criterion	Importance
Relevant operational expertise/costings Relationship/company size	*****
Contract terms Experience	****
Service levels/technical capability Relevant sector experience	***

Source: INPUT

At present, one of the key screening criteria is the ability of the vendor to provide good value for money in matching the operational requirements of the client. Typically, a wide range of vendors should pass this test. Clients need to perceive that the vendor has the appropriate range of operational capability to match their IT infrastructure. Often this will not be a very demanding test should the client, for example, wish to outsource a single, medium-sized IBM data centre. However, it becomes more demanding as the client increases the variety of technologies and the geographic scope of the requirement. For example, BP Exploration decided that it required a consortium of vendors in order to outsource a global infrastructure containing mainframes, wide-area networks and desktop devices. In addition, the vendor must be able to meet the required service levels within this architectural framework.

Clients need to feel that their choice of vendor is risk-free and to perceive that the scale of the vendor is appropriate. This can lead to vendors being perceived to be either too large or too small for the client. For example, the majority of vendors were perceived to be too small for safety by the Inland Revenue. Many small to medium-sized organisations perceive that they would be unable to influence, or would receive a second class service from, one of the major outsourcing vendors. Clients are most comfortable choosing vendors with whom they have an existing relationship or, failing this, who have a good market reputation.

Relevant industry sector and process experience are becoming of growing importance as organisations seek more than infrastructure management capability and demand vendors that can assist them in making the best use of IT to support their business development.

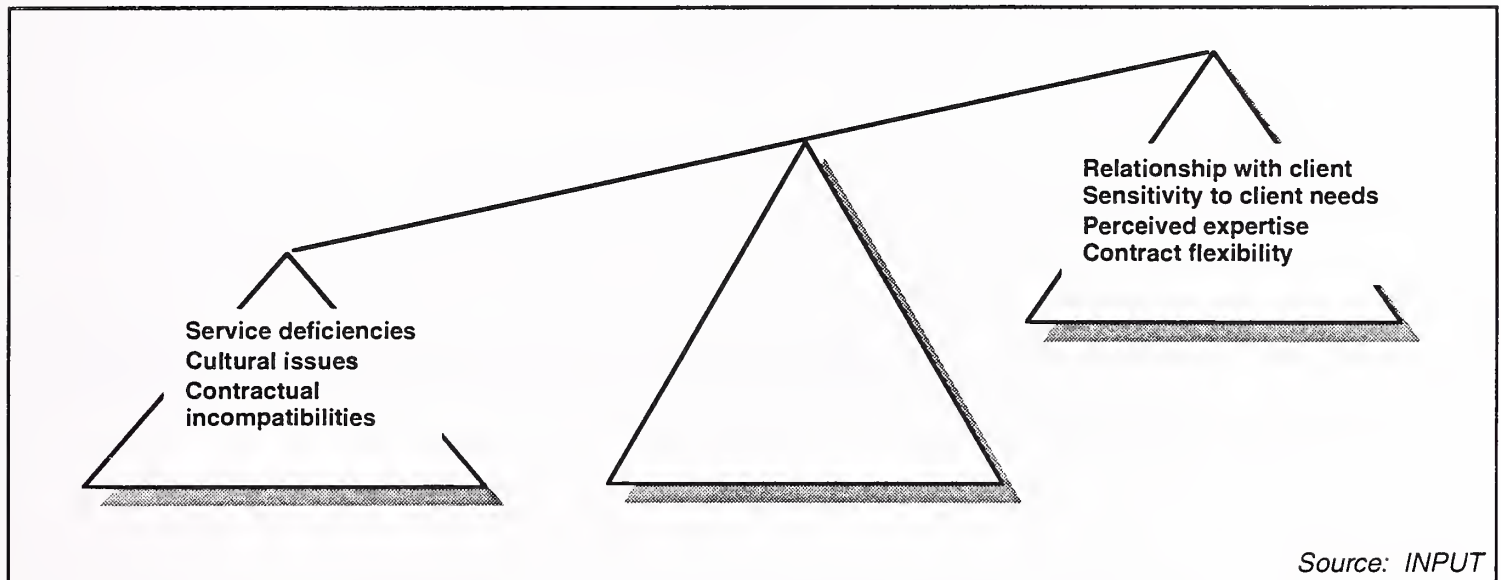
With many of these criteria, it may be difficult to differentiate between vendors and hence decide the outcome of the bid. Some factors, such as overall service capability, should be satisfied by the majority of vendors in

the tendering process. Other factors are more important in enabling clients to choose between vendors.

Some of these factors are listed in Exhibit II-5.

Exhibit II-5

Key Criteria Influencing Bid Outcome



The factors on the right-hand side of the scales are critical in enabling clients to make a positive decision in favour of a vendor. Those on the left are used to eliminate vendors from the bidding process.

The factor mentioned most frequently as the reason for choosing the selected vendor is the prior existence of a relationship between client and vendor. This factor assists equipment vendors in penetrating the outsourcing market, particularly when it is coupled with perceived strong operational expertise with their own equipment and systems software.

In practice, clients typically find it easier to exclude a vendor on the grounds of a perceived shortfall in technical capability rather than use technical capability as a positive reason for choosing a particular vendor. Specific criteria used to exclude vendors include:

- Lack of relevant platform or operating environment expertise
- Inadequate geographic match - particularly relevant for desktop services outsourcing and other highly distributed environments
- Lack of business knowledge or experience in key industry-specific applications

Potentially, the most critical area where contracts can be both won and lost is the vendor's sensitivity to the client's needs and the vendor's willingness to reflect this flexibility in the contract terms.

Contracts can be won by vendors who share the client's vision of the services required, pay considerable attention to detail and provide a high level of flexibility in terms of contract duration and options. For example, CFM claim to have won a contract for which they failed to make the shortlist by offering to take a 15-year property lease alongside a 5-year outsourcing agreement.

On the other hand, contracts can be lost by vendors who endeavour to impose their vision and contract terms on the client. Clients are scared of losing control of the vendor once the contract has been signed and will often favour vendors who take steps to assure the client that they can offer an element of flexibility in the terms and duration of the contract they propose. Contract break points and termination terms can be particularly important in this respect.



Need For New Systems Causes CFOs To Investigate Outsourcing

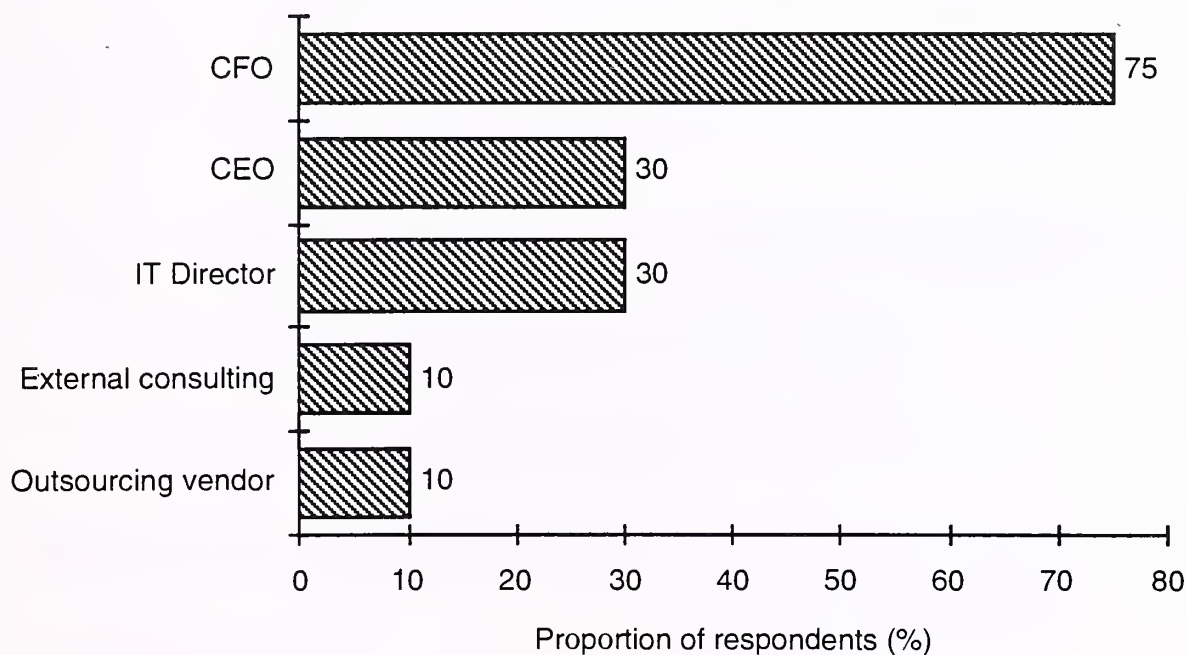
A

Chief Financial Officers Initiate IS Outsourcing

Exhibit III-1 lists the perceived importance of the parties shown in promoting the use or evaluation of IS outsourcing.

Exhibit III-1

Principal Initiators of Outsourcing: Europe



Standard error = 6%

Sample of 55 respondents

Source: INPUT

Chief financial officers were regarded as being very influential in promoting the use or evaluation of IS outsourcing by a broad majority of respondents across the senior management team.

Historically, a large proportion of IT departments reported directly to the chief financial officer. This reporting relationship has now frequently changed, with the appointment of IT directors reporting directly to the chief executive officer or main company board. Nonetheless, CFOs still tend to maintain closer links to the IT function than their fellow directors, including chief executive officers.

Consequently, they tend to be quicker than their colleagues in identifying the need for external assistance in developing their organisations' use of information technology.

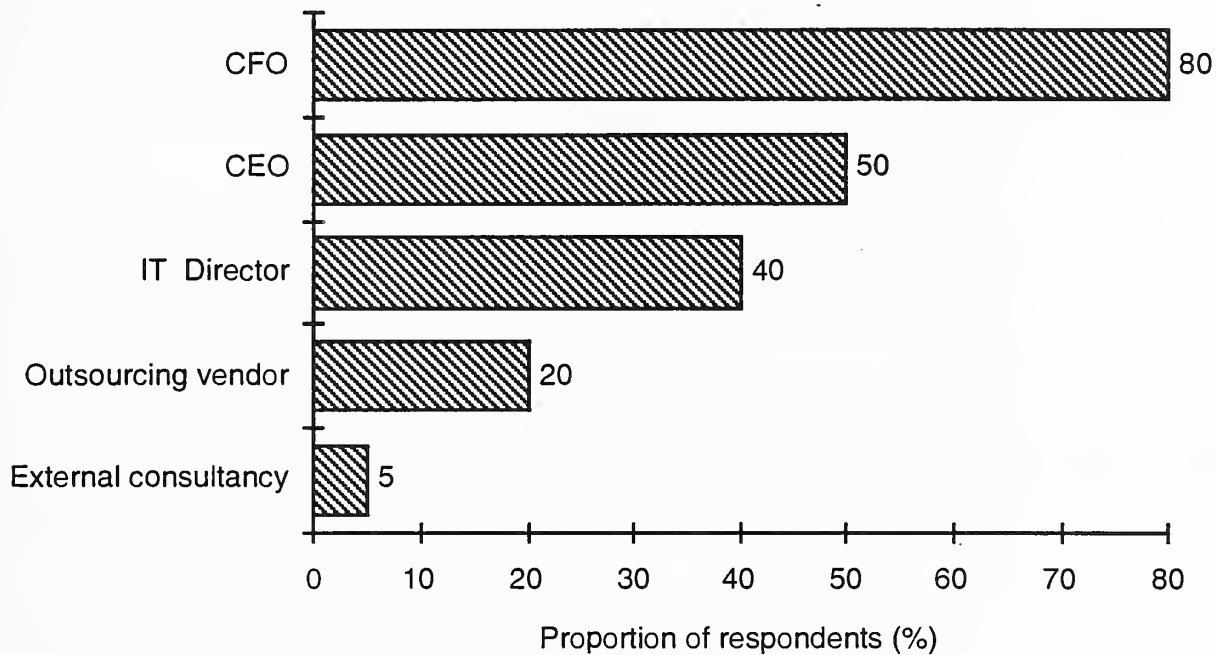
Chief executive officers take a more remote view of their IT functions and are much less likely than CFOs to instigate an appraisal of IS outsourcing.

The overall influence of external consultancies in initiating IS outsourcing is perceived to be low. Consultancies are more typically used to assist organisations in deciding the pattern of functions to be outsourced and the choice of vendor, once the decision to adopt IS outsourcing has been made in principle by the senior management team. However, management consultancies stressing the importance of business reengineering and core business focus are potentially significant influences in favour of IS outsourcing on the senior management team.

Similarly, outsourcing vendors are perceived to have a relatively low level of importance in instigating investigations of IS outsourcing. Indeed, the majority of outsourcing vendors in Europe tend to react to requests for proposals, or informal discussions, on outsourcing from potential prospects. The sales style of making direct approaches to board directors of companies is favoured by only a small number of large vendors targeting the largest organisations in Europe.

Exhibits III-2, III-3 and III-4 show the perceived importance of each of the principal initiators of outsourcing for France, Germany and the UK respectively.

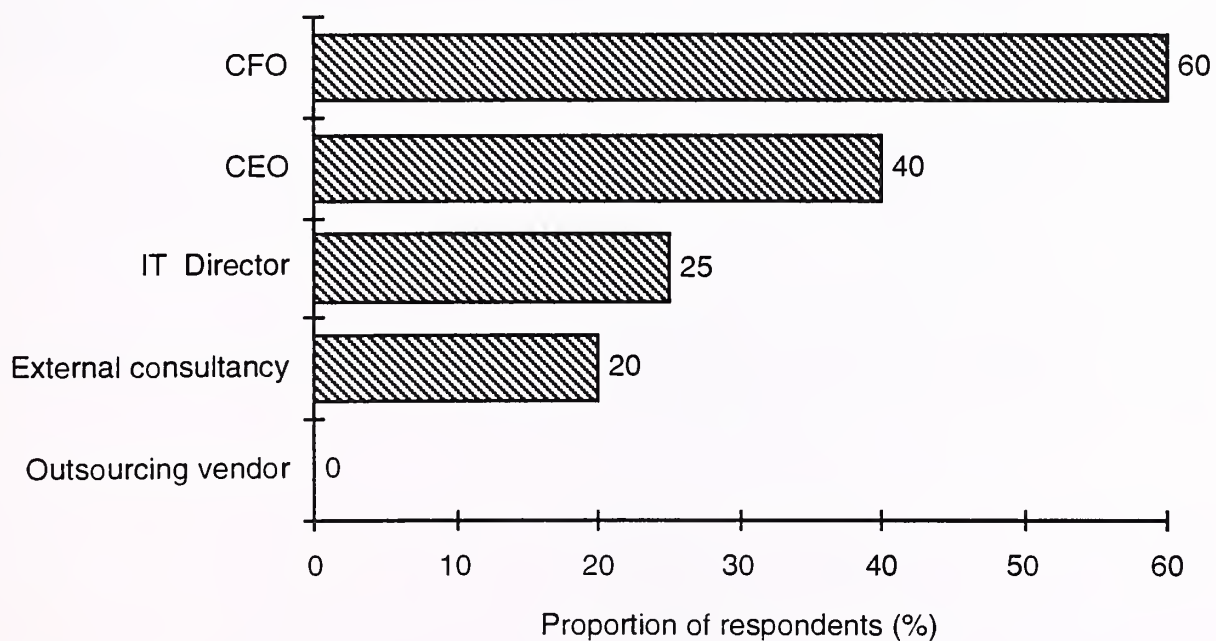
Exhibit III-2

Principal Initiators of IS Outsourcing: France

Standard error = 10%

Source: INPUT

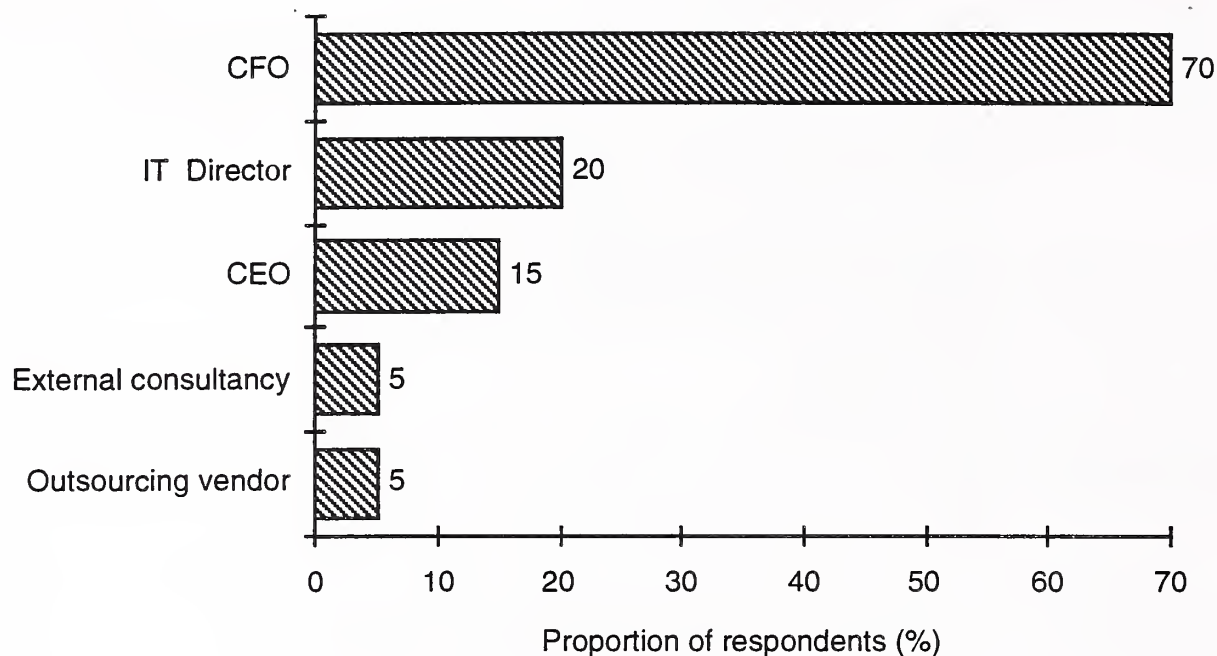
Exhibit III-3

Principal Initiators of IS Outsourcing: Germany

Standard error = 15%

Source: INPUT

Exhibit III-4

Principal Initiators of IS Outsourcing: UK

Standard error = 9%

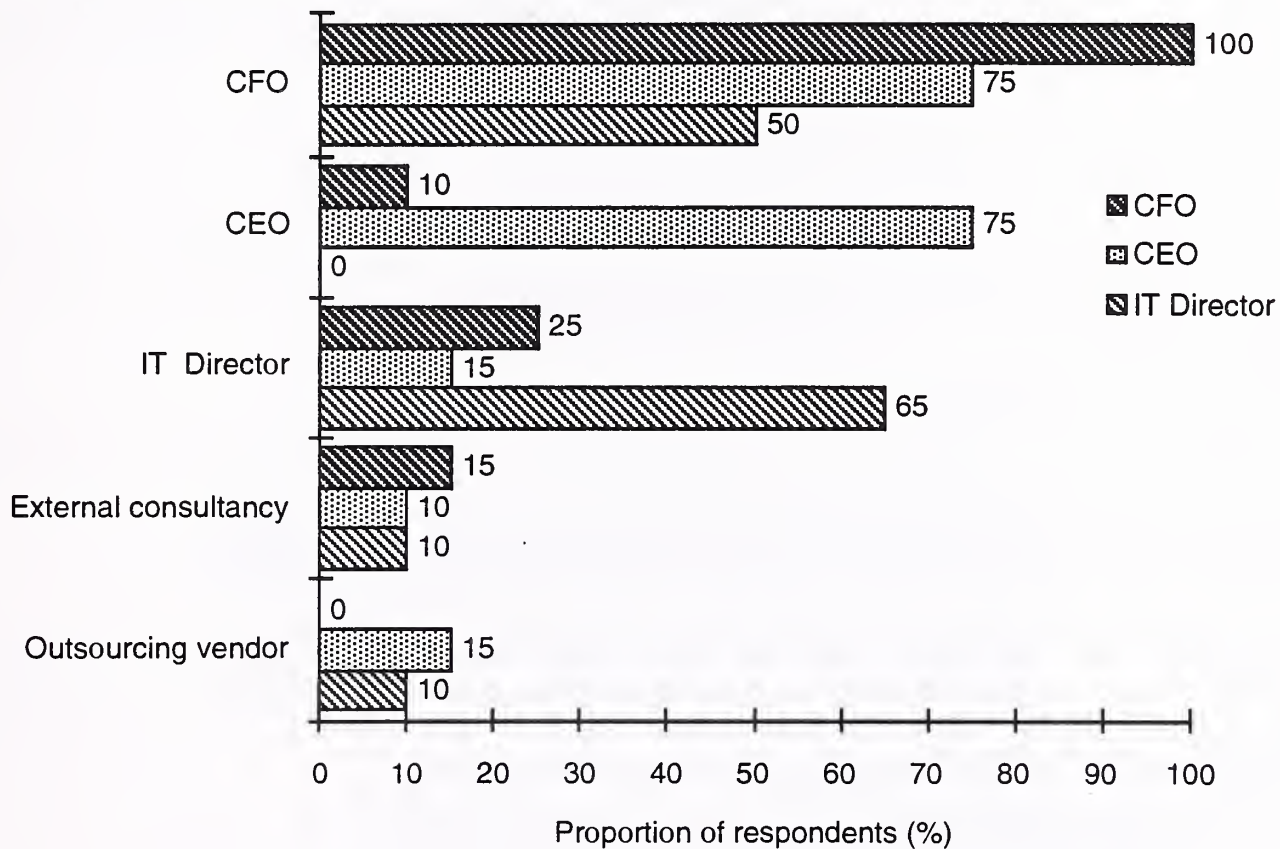
Source: INPUT

The perceived pattern of influence is broadly similar across these three countries. The main difference is the relative lack of influence of chief executive officers in the decision to use or evaluate IS outsourcing within the UK, where this process appears to be overwhelmingly dominated by chief financial officers.

The decision to investigate IS outsourcing appears to be much more of a team decision in France and Germany, where there is greater involvement of chief executive officers and IT directors/managers at this early stage.

Exhibit III-5 shows the differing perspectives of the main players on the pattern of influence at this stage.

Exhibit III-5

Principal Initiators of Outsourcing by Respondent Type

Standard error = 10%

Sample of 55 respondents

Source: INPUT

Both IT managers and CFOs perceived themselves to be the most important instigators of IS outsourcing within their organisations.

There may be an element of objectivity in the individual assertions behind this finding, since the interviewer would tend to be directed towards the major decision-maker in the outsourcing process within each organisation. However, in this situation, it is interesting to compare respondents' views of the relative influence of the other parties.

Using this criterion, chief financial officers are again identified as being the most important influences in the initiation of IS outsourcing. Chief financial officers were regarded as major influences in the decision to adopt IS outsourcing by the majority of IT directors and chief executive officers. Indeed, a slightly greater proportion of chief executive officers regarded their CFOs as important instigators of IS outsourcing than regarded themselves as important at the initiation stage.

Only a minority of chief financial officers and other senior executives regarded their IT directors or managers as important initiators of IS outsourcing. In addition, the distance between IT functions and chief executive officers is illustrated by the fact that none of the IT directors interviewed perceived the chief executive officer to be an important influence in initiating IS outsourcing, an opinion largely shared by the overwhelming majority of CFOs.

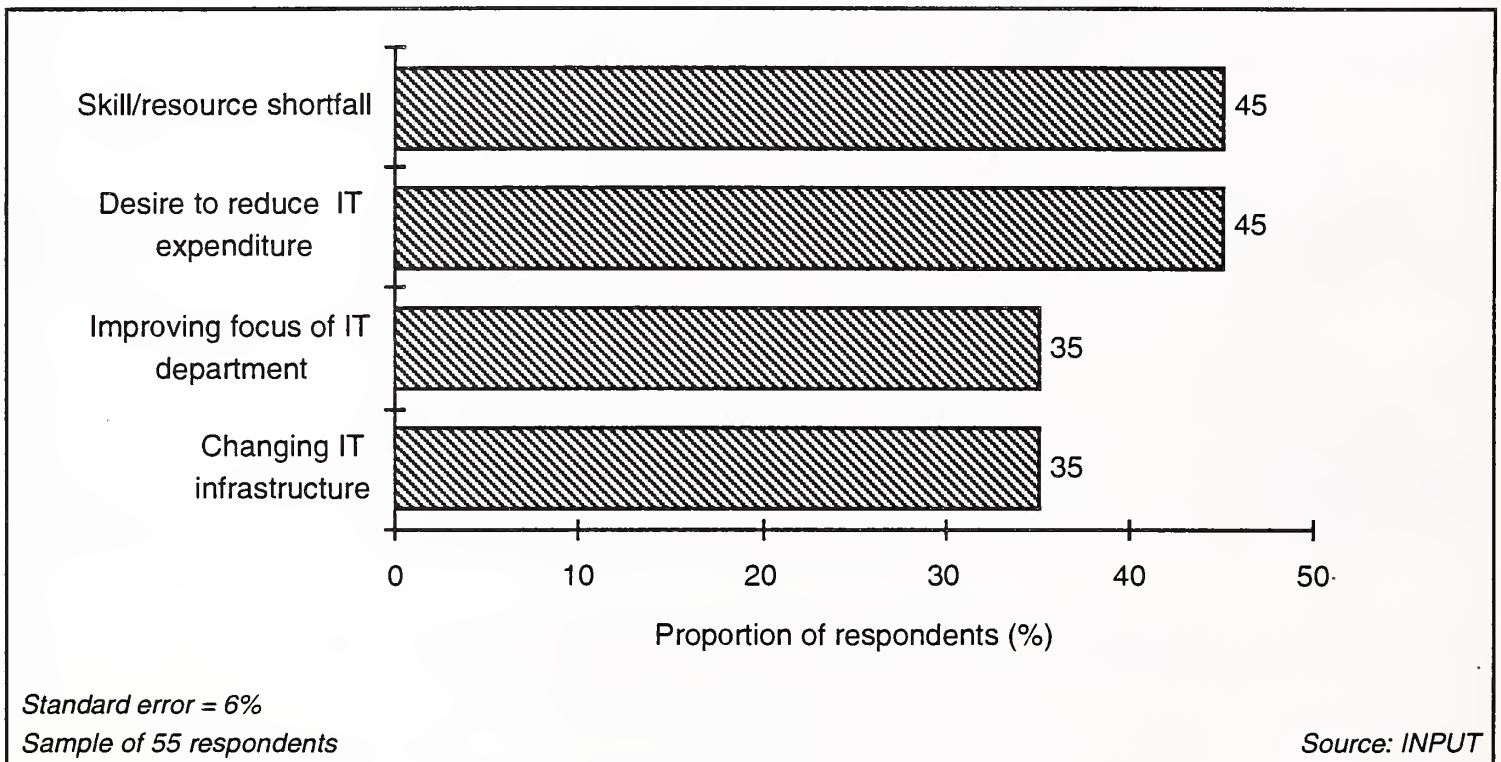
B

Outsourcing Occurs Against a Background of Skill Shortages

The principal circumstances surrounding decisions to evaluate or use IS outsourcing are listed in Exhibit III-6.

Exhibit III-6

Background to IS Outsourcing: Europe



As expected, the desire to reduce, or stabilise, IT expenditure is one of the major driving forces behind IS outsourcing. This is particularly the case where the overall organisation is having financial difficulties (for example, British Aerospace or FAG Kügelfisher) and needs to reduce expenditure wherever possible. In these circumstances, outsourcing computer data centres can produce both short-term cost savings and an immediate cash injection. This cash injection can be used to reduce the organisation's level of borrowing, assist in financing a restructuring of the existing core business, or finance a much-needed systems redevelopment programme.

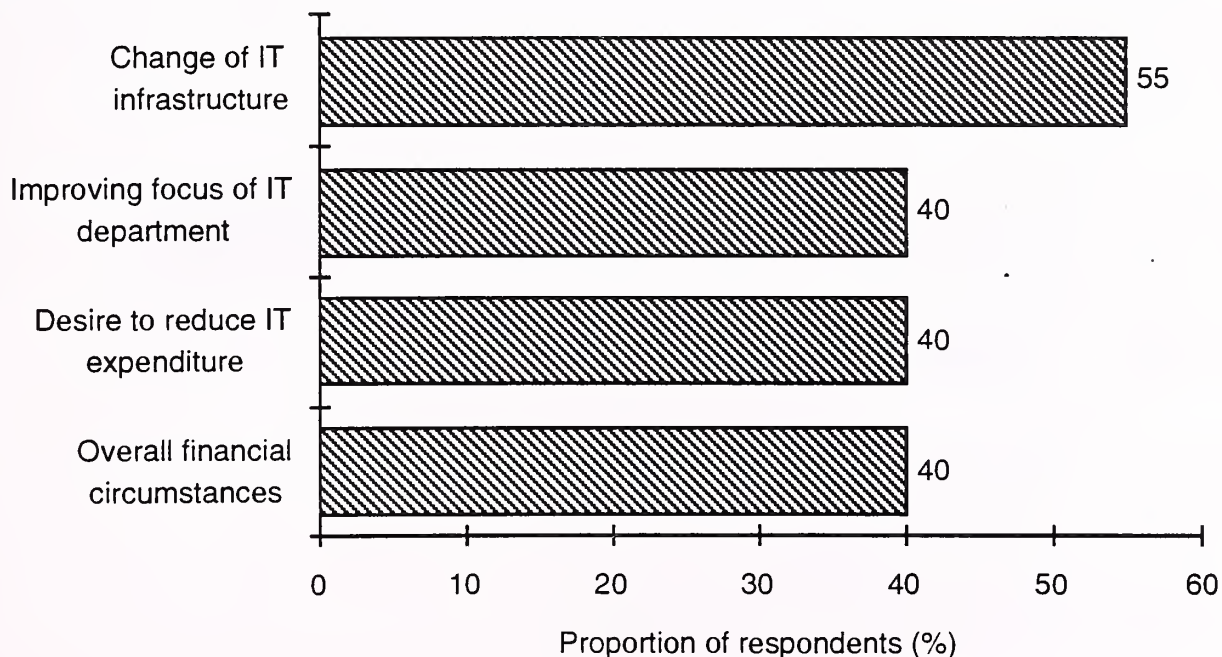
However, cost reduction is not the overwhelming reason for organisations' adoption of IS outsourcing. Other factors are also extremely important. One of these is the change in IT infrastructure. Change in IT infrastructure creates considerable strains within the in-house IT department. In this situation, the in-house IT department is faced with the challenge of supporting the existing infrastructure and applications used within the company, while simultaneously designing, developing, integrating and implementing the new architecture and applications.

Outsourcing has been used traditionally as a means of off-loading the operation and support for existing systems, thus enabling the in-house IT department to concentrate its efforts on new systems development. In addition, outsourcing is a means by which organisations can acquire the necessary specialist expertise and skills in the new technologies being adopted for the future.

Exhibits III-7, III-8 and III-9 list the principal circumstances surrounding decisions to evaluate or use IS outsourcing in France, Germany and the UK respectively.

Exhibit III-7

Background to IS Outsourcing: France



Standard error = 10%

Source: INPUT

Exhibit III-8

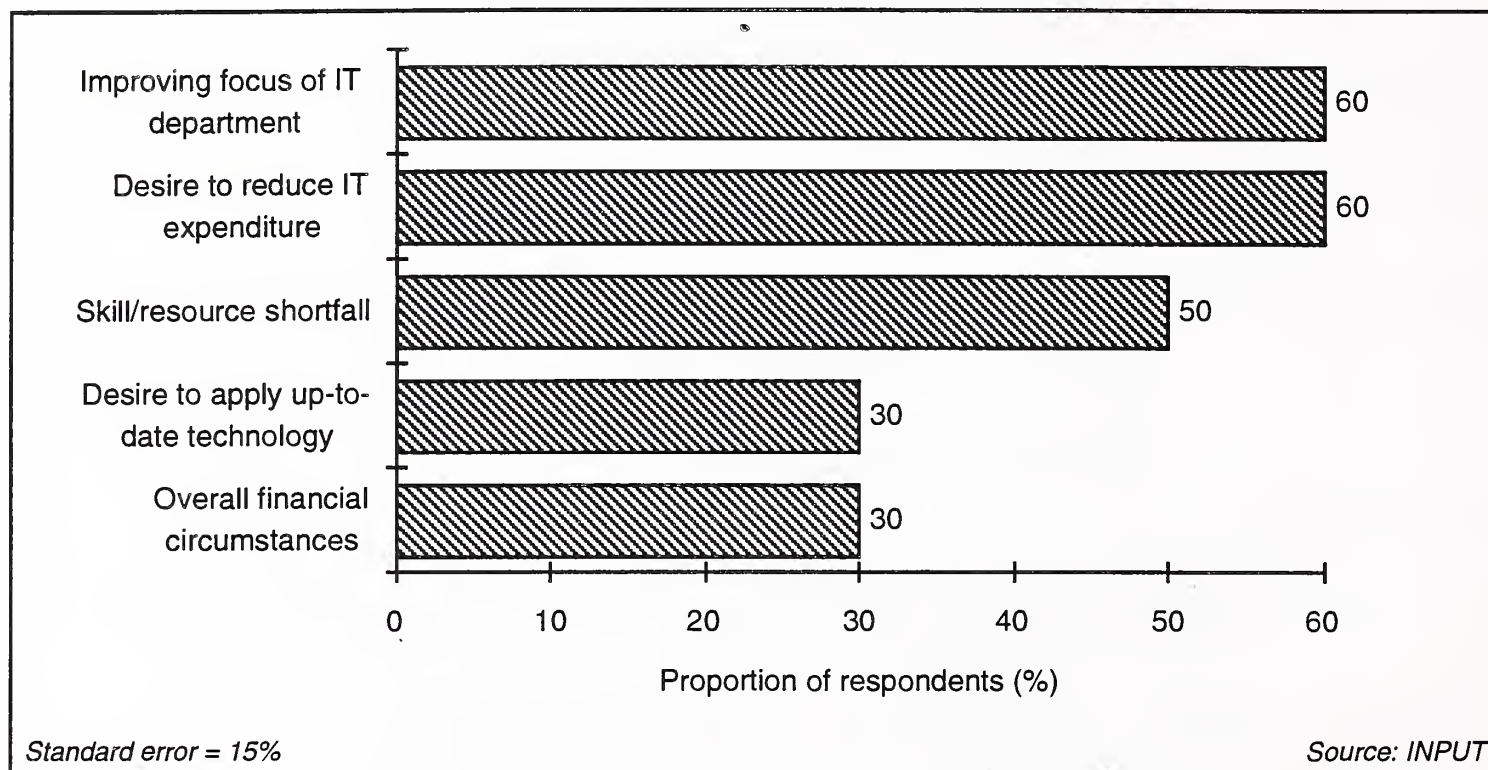
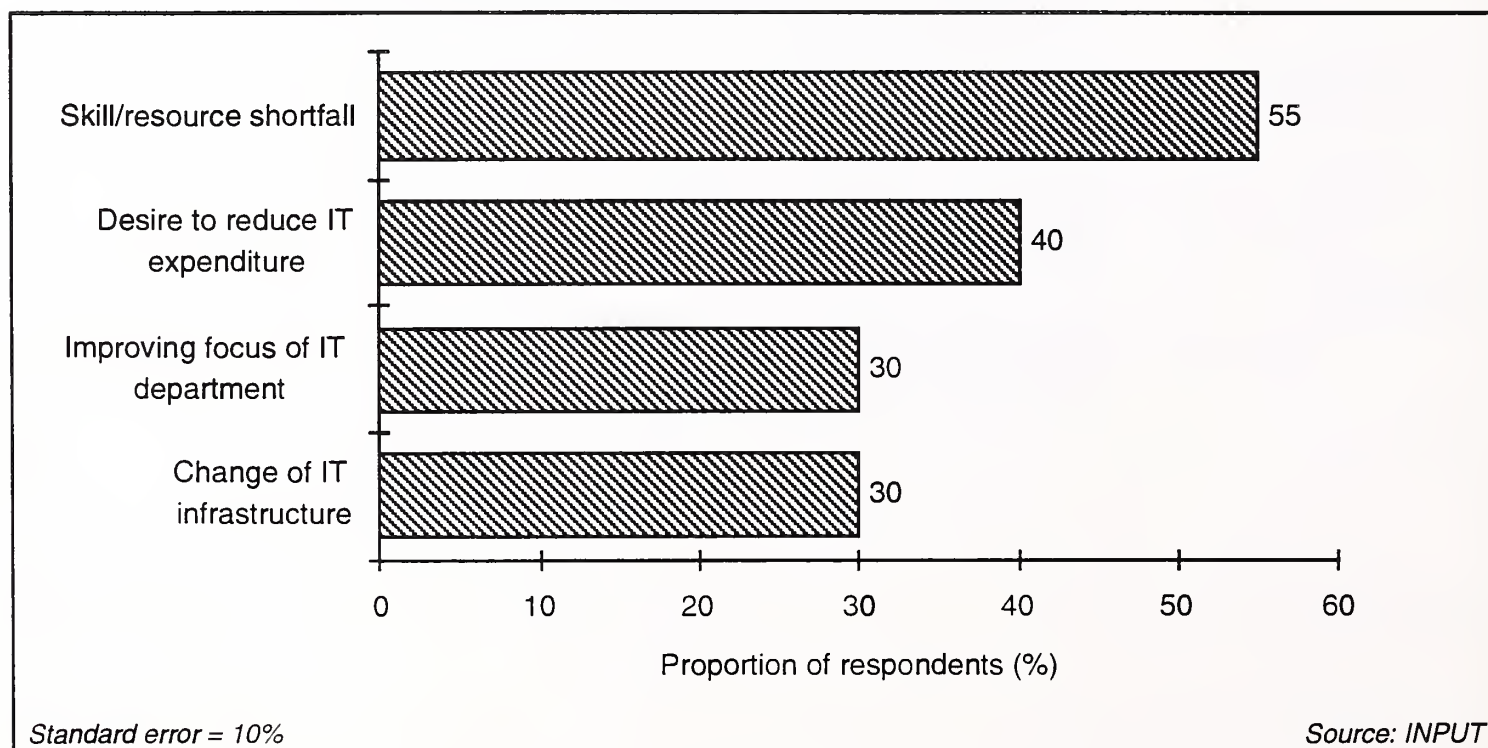
Background to IS Outsourcing: Germany

Exhibit III-9

Background to IS Outsourcing: UK

The broad themes behind the adoption of IS outsourcing in each country are similar. However, there are also some subtle differences in emphasis between the countries.

In France, the main emphases are on assisting IT departments in migrating to more responsive IT infrastructures while simultaneously reducing the organisation's IT expenditure. In Germany, similar concerns are expressed in terms of the desire to apply up-to-date technology to the business, and in overcoming the corresponding skill shortfall, while simultaneously reducing the organisation's IT expenditure. In the UK, IT budgets and headcounts have suffered considerable pressure over the past three years. This has also had an adverse impact on the ability of in-house IT departments to retrain their personnel in the latest technologies. Staffing has also been reduced in many organisations. Consequently, the major emphasis is on meeting the gap in skills and resources necessary to utilise the new technologies.

Exhibit III-10 identifies the principal and supporting factors leading to IS outsourcing, viewed from the differing perspectives of chief financial officers, other senior executives and IT directors.

Exhibit III-10

Reasons for IS Outsourcing by Respondent Type

	Chief Financial Officers	Other Senior Executives	IT Directors/Managers
Principal Factors	Skill/resource shortfall Change of IT infrastructure	Desire to reduce IT expenditure Change of IT infrastructure	Skill/resource shortfall Improving focus of IT department
Supporting Factors	Desire to reduce IT expenditure Corporate restructuring Improving focus of IT department	Improving focus of IT department Overall financial circumstances Corporate restructuring Skill/resource shortfall	Desire to reduce IT expenditure Overall financial circumstances Desire to apply up-to-date technology

Source: INPUT

The personnel for whom reducing the organisation's overall IT expenditure is the single most important reason for evaluating outsourcing are chief executive officers and other non-financial senior executives. These are also the personnel who show the highest propensity to be influenced in favour of outsourcing by sales approaches from outsourcing vendors. Corporate restructuring, including the adoption of a core business focus, is also most likely to be a significant factor behind a move to outsourcing for this group of personnel.

On the other hand, the most important reason for adoption of IS outsourcing, as perceived by chief financial officers and IT directors, is a shortfall in IT skills or resources. Surprisingly, cost reduction was rated only third by CFOs as a reason for adopting outsourcing. Overall, CFOs appear to be more concerned with renewing the technology used within the business. Indeed, for all senior executives, including CFOs, a change in IT infrastructure is a major factor in their decision to evaluate IS outsourcing.

IT directors appear to turn to outsourcing when faced with a combination of the challenge to introduce more up-to-date technology to the business within significant headcount and budgetary constraints. This forces the organisation to identify its own immediate priorities and to outsource those activities that it lacks the expertise to handle together with those that are not critical to its future success within the enterprise.

C

Outsourcing is Triggered by a Major Systems Development Need

Exhibit III-11 lists the proportion of respondents by country that perceive their organisation's use of IS outsourcing to have been triggered by a specific event.

Exhibit III-11

Extent to Which Outsourcing was Triggered by a Specific Event by Country

Country	Proportion of Instances Triggered by Specific Event (%)
France	80
Germany	70
UK	30
Europe	55

Source: INPUT

Overall, the majority of respondents perceived that their organisation's use of outsourcing had been triggered by a specific event, rather than a general background need to reduce costs. This belief was particularly prevalent amongst respondents in France and Germany.

Exhibit III-12 provides a breakdown by respondent type of the extent to which respondents perceived that their organisation's use of IS outsourcing had been triggered by a specific event.

Exhibit III-12

**Extent to Which Outsourcing was Triggered by a Specific Event
by Respondent Type**

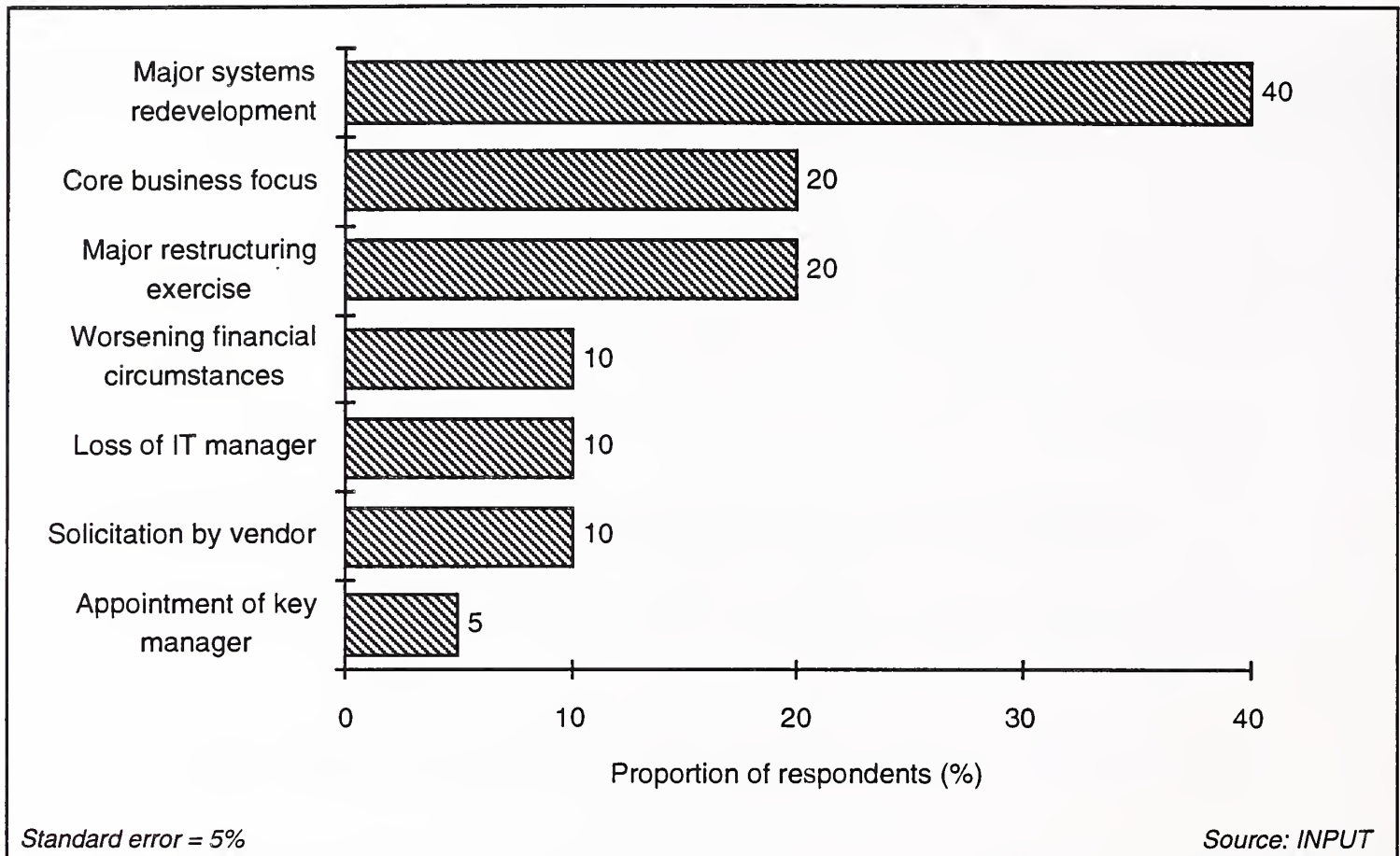
Respondent Type	Proportion of Instances Triggered by Specific Event (%)
Chief financial officers	70
Other senior executives	60
IT directors/managers	40
Overall	55

Source: INPUT

The majority of chief financial officers and other senior executives, including chief executive officers, take the view that IS outsourcing is typically triggered by a specific event. Since CFOs tend to be the principal instigators of IT outsourcing, it can safely be concluded that this is, in fact, typically the case.

Exhibit III-13 lists the principal events that respondents perceived to be instrumental in their organisation's adoption of IS outsourcing.

Exhibit III-13

Triggers for Outsourcing: Europe

The single most important event that triggered the need to evaluate IS outsourcing was a major systems development project. The imminent need for the implementation of major new systems, frequently using IT technologies or architectures with which the organisation has little prior experience, causes many organisations to seek external help. If the organisation also faces tight headcount restraints, then it also forces the in-house IT department to make a choice between the activities it is prepared to subcontract and those it wishes to retain in-house.

Company restructuring and relocation are also important in initiating evaluation of outsourcing as is a change in senior company management or a change in company ownership. Major restructuring often involves the re-organisation of the company into a flatter structure and the creation of a number of business units with increased autonomy. A major review of internal business processes, and hence existing IT systems, was also mentioned as a driving force behind the adoption of IS outsourcing.

Some business units may be sold to new owners. This often results in separating the business unit from its former corporate supplier of IT services and necessitates the search for a new supplier. The consequence is frequently a need for mainframe data centre services in the short-term to run the existing corporate systems. In the longer term, the organisation will frequently wish to redevelop its own systems, probably using new applications and architectures.

Although the appointment of new chief financial officers can be a source of concern for IT managers, and there are some examples of CFOs with a track record of favouring IS outsourcing, a more significant factor is often the loss of, or fear of over-dependency on, key senior IT personnel.

Exhibits III-14, III-15, and III-16 list the principal triggers for outsourcing identified by respondents in France, Germany and the UK respectively.

Exhibit III-14

Principal Triggers for Outsourcing: France

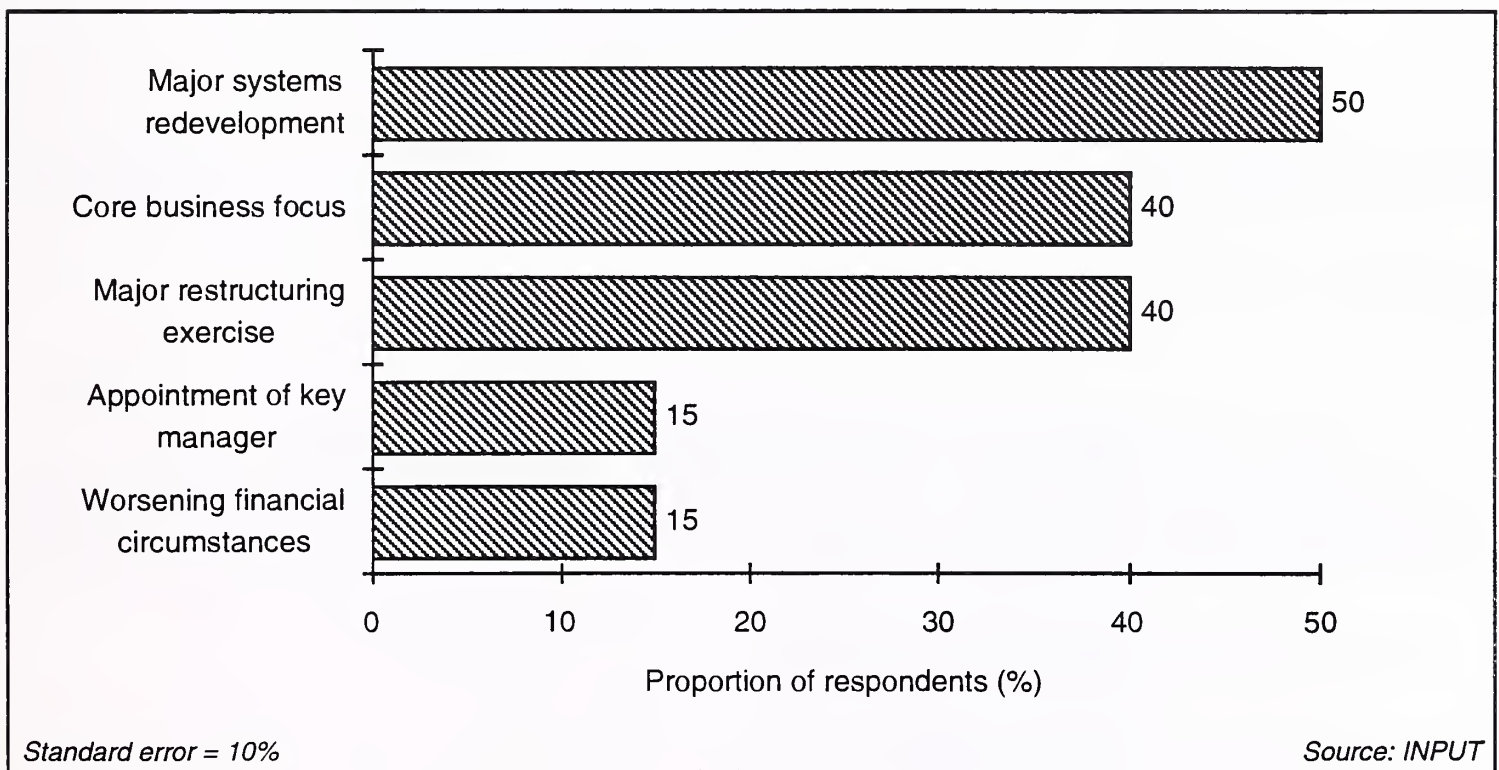
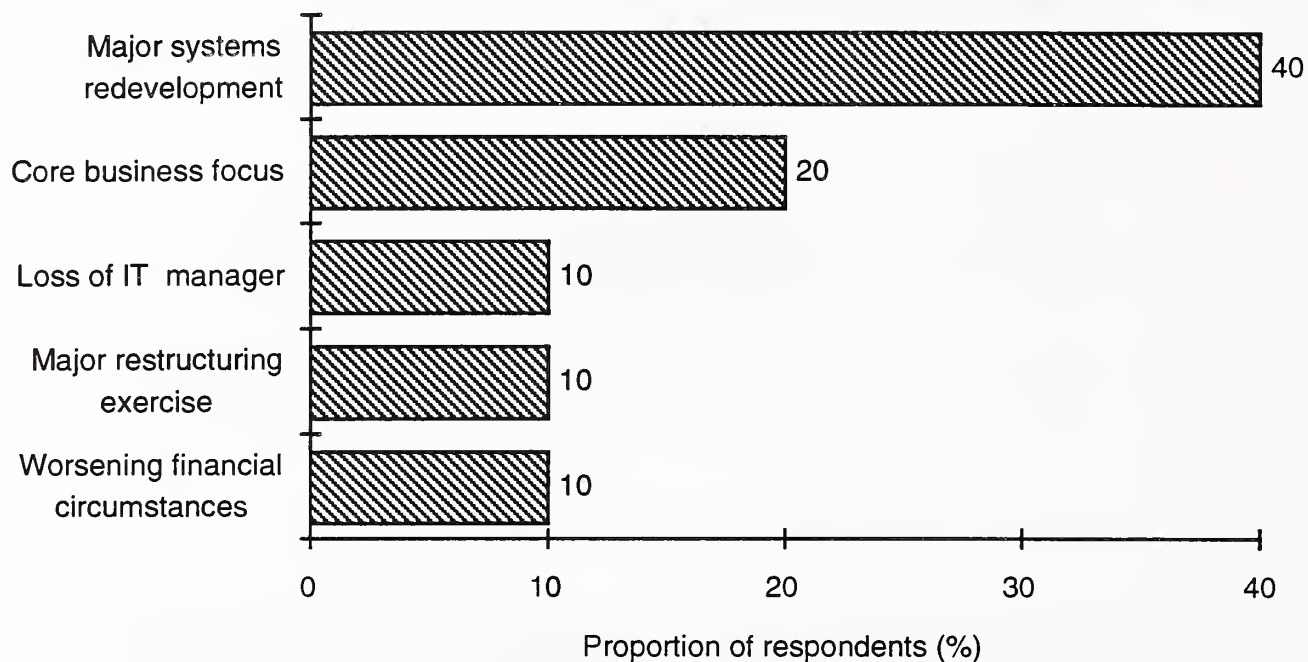


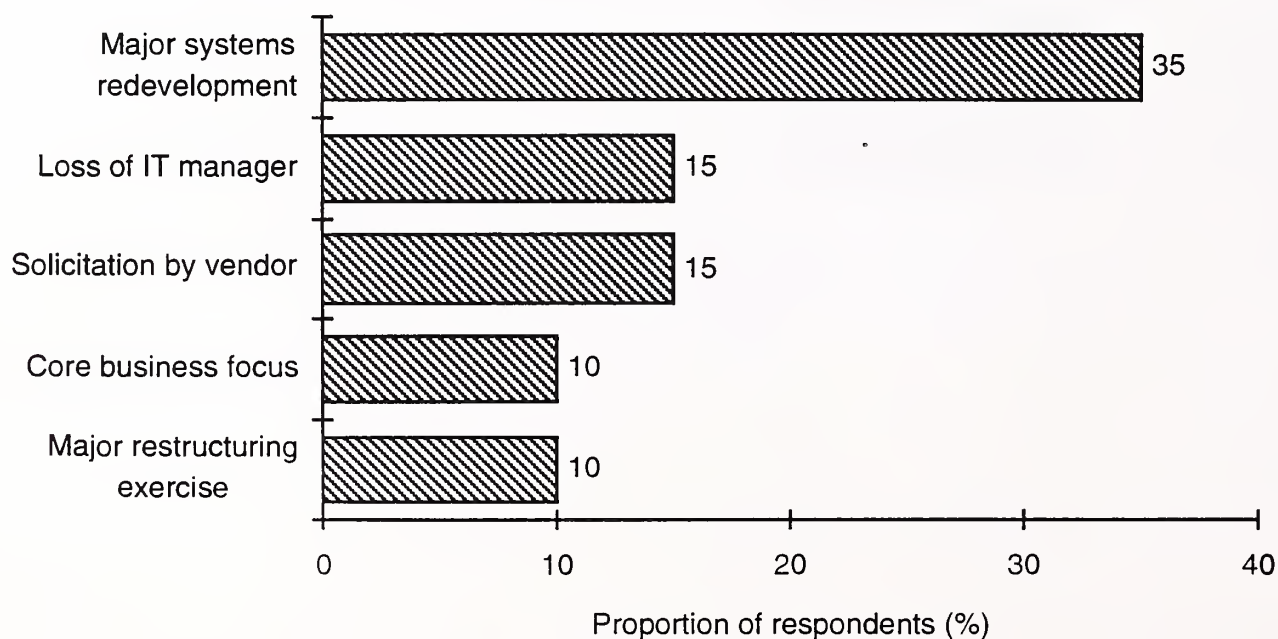
Exhibit III-15

Principal Triggers for Outsourcing: Germany

Standard error = 15%

Source: INPUT

Exhibit III-16

Principal Triggers for Outsourcing: UK

Standard error = 10%

Source: INPUT

The most significant factor in triggering use of IS outsourcing is reported to be the need for major systems development in each of the three countries. Much of this need for redevelopment is being initiated by extensive corporate restructuring. While this applies to a certain extent to each of the countries, it is a particularly strong trigger for outsourcing in France.

Overall, solicitation by outsourcing vendors is perceived to be the trigger for outsourcing in only a minority of instances. However, it appears to be a more successful strategy in the UK than elsewhere in Europe. At least in the UK, vendors should consider promoting outsourcing services to senior executives within organisations that have recently lost their IT directors/managers or other key IS personnel. One strategy would be to promote the level of outsourcing appropriate to the perceived management shortfall. For example, the loss of the IT director could be used as an opportunity to promote applications operations services; loss of key operations personnel could lead to openings for platform operations or other infrastructure management services, and loss of key development personnel could create openings for applications management services.

In addition, differing personnel have differing perceptions of the key triggers for outsourcing and are likely to be motivated to adopt outsourcing on the basis of different pressures. Exhibit III-17 provides a breakdown of user perceptions of the key triggers for adoption of outsourcing by respondent type.

Exhibit III-17

Triggers for Outsourcing by Respondent Type

	Chief Financial Officers	Other Senior Executives	IT Directors/Managers
Principal Trigger	Major systems development	Core business focus	Major systems development
Secondary Triggers	Loss of IT manager Major restructuring exercise	Major systems development Worsening financial circumstances Major restructuring exercise	Core business focus Major restructuring exercise

Source: INPUT

Chief financial officers, perhaps reflecting their closer day-to-day involvement with IT than other senior executives, primarily take a pragmatic view of the need to adopt outsourcing based on the need to resource the development of new systems and the disruption caused by the loss of key IT personnel. Alternatively, the departure of senior IT managers presents an opportunity to review the possibility of outsourcing with reduced organisational conflict.

On the other hand, non-financial senior executives view IS outsourcing more theoretically in terms of reengineering the organisation to improve its core business focus.

Again this suggests that different messages should be promoted to CFOs as against other members of the board. Non-financial senior managers will be more receptive to outsourcing when undergoing major organisational changes and when benchmarking their capabilities as an organisation.

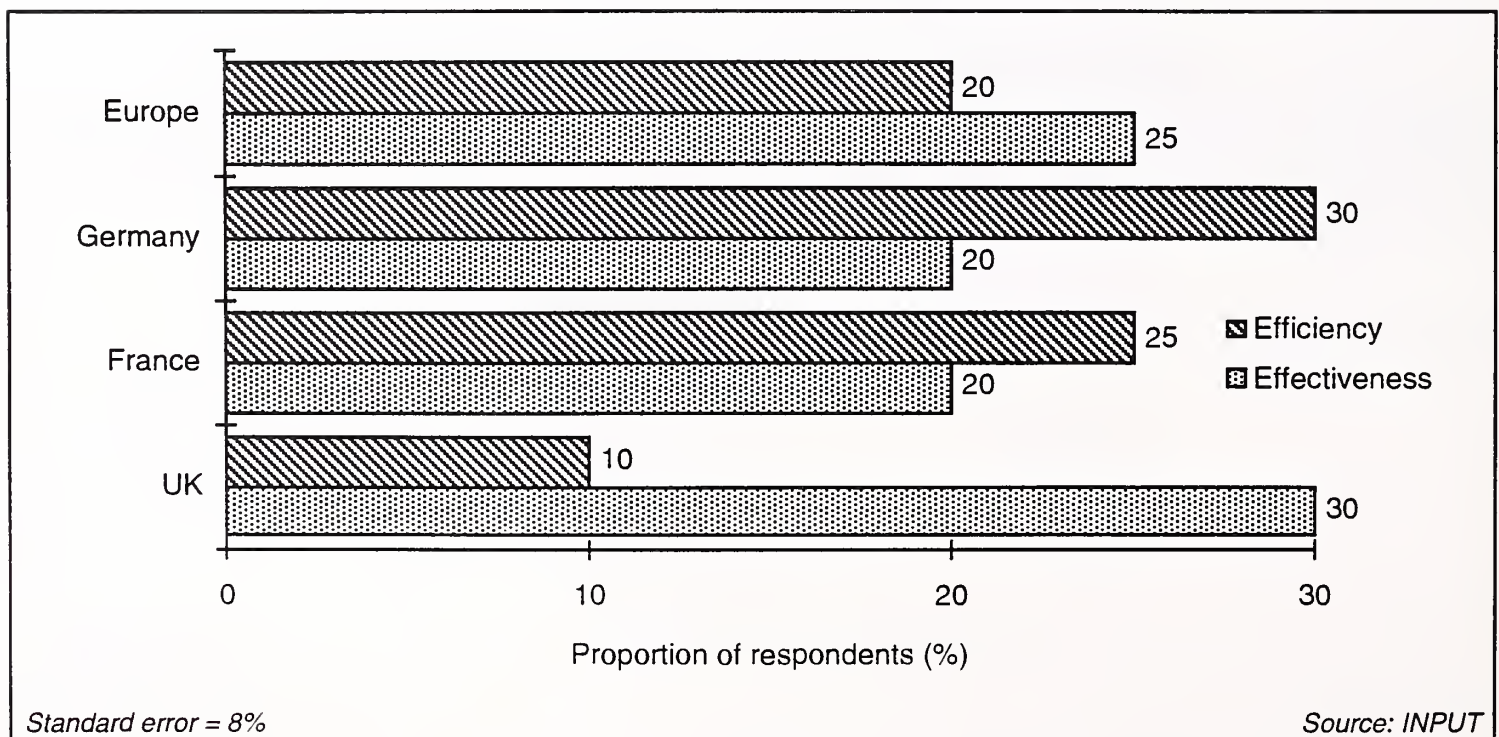
D

CFOs Perceive Low Value For Money from IT Departments Subject to Outsourcing

Exhibit III-18 shows the proportion of respondents who perceived their in-house IS department to be highly efficient or effective prior to the adoption of outsourcing.

Exhibit III-18

IT Efficiency and Effectiveness Prior to Outsourcing by Country

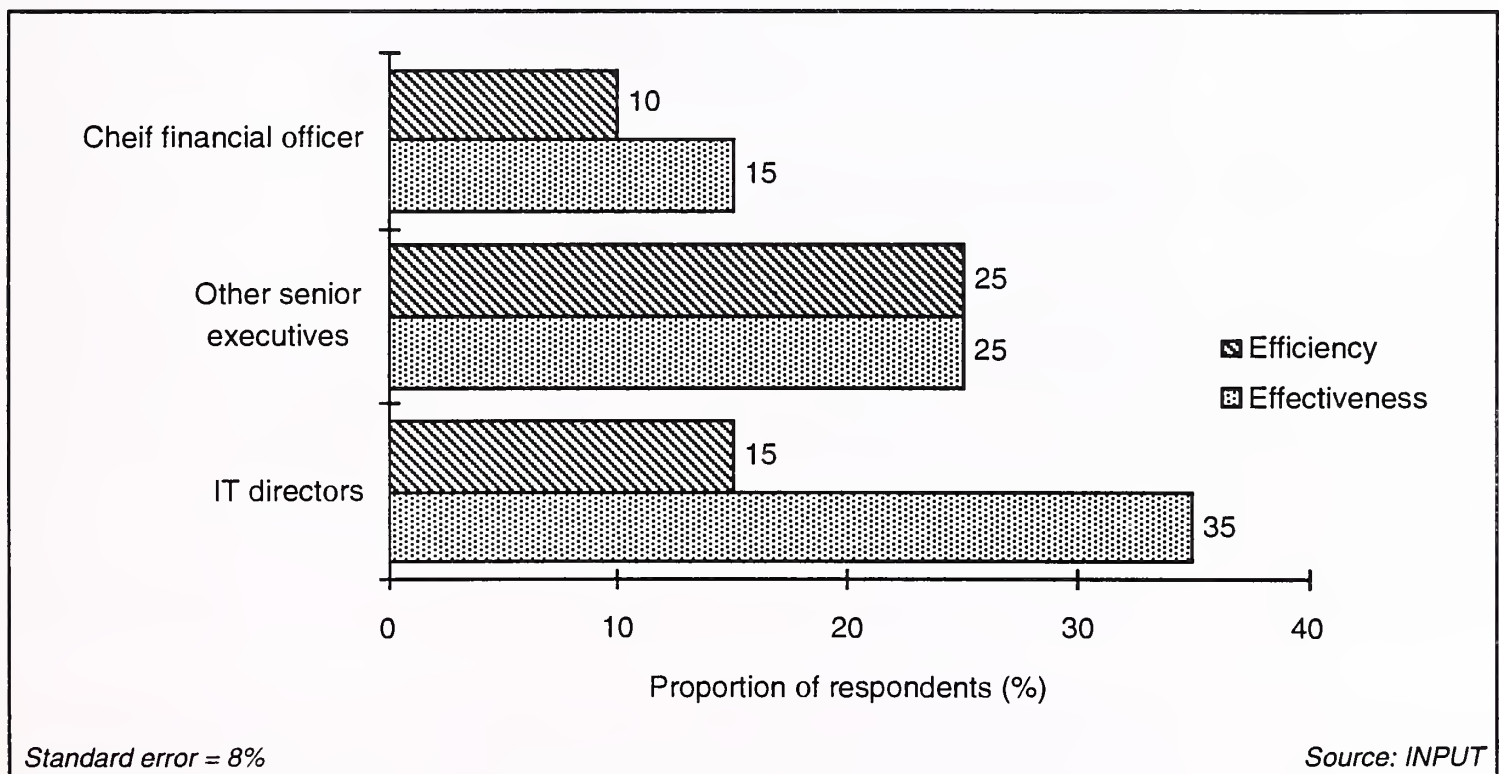


Overall the proportions of executives, including IT directors and managers, who consider their in-house IT departments to be highly efficient or highly effective is a small minority. However, it is difficult to identify these criteria as key determinants of outsourcing on an individual company basis. Earlier studies (*Impact of Reengineering on IS Outsourcing - Europe, 1994*) indicated that only 25% of executives in European organisations which have not yet adopted IS outsourcing perceived their in-house IT departments to offer a high level of cost-effectiveness. On this basis, there is no clear difference in perception of efficiency between organisations that have outsourced elements of their IT function and those that have not.

Exhibit III-19 shows the proportion of respondents who perceived their in-house IS department to be highly efficient or effective prior to the adoption of outsourcing, broken down by respondent type.

Exhibit III-19

Perceived IT Efficiency and Effectiveness Prior to Outsourcing by Respondent Type



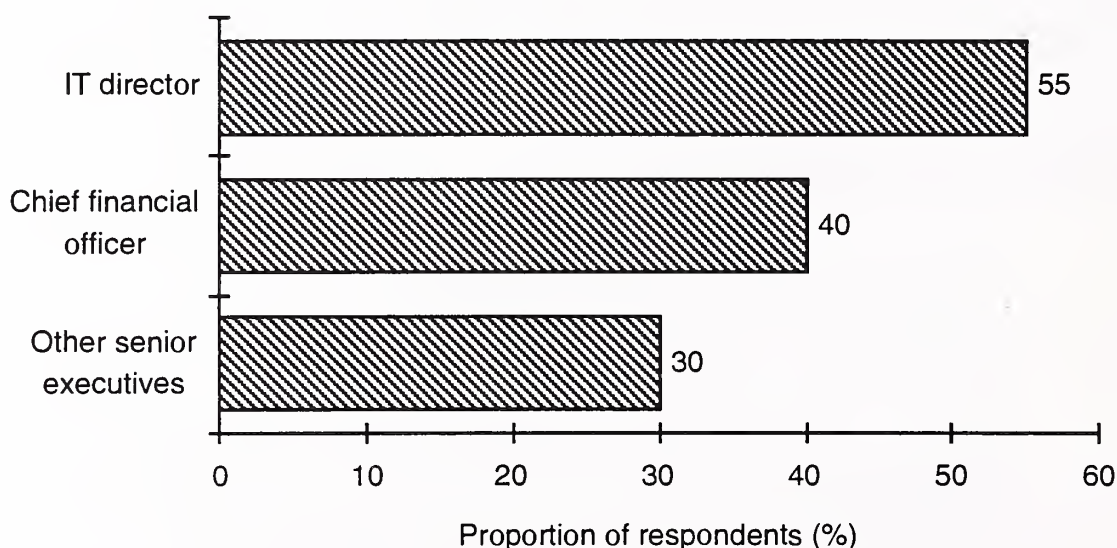
Surprisingly, even IT directors/managers typically perceived the efficiency of their IT departments to be relatively low. However, a much higher proportion of IT directors and managers perceived the effectiveness of the IT department to be high. On the whole, this view was not shared by CFOs, the overwhelming majority of whom perceived their IT departments prior to outsourcing as providing poor value for

money in terms of both their efficiency and their effectiveness. Indeed, it may be that perceived low effectiveness is a better determinant of outsourcing than efficiency. If the CFO, who is the prime initiator of IS outsourcing, perceives the in-house organisation to be ineffective as well as inefficient then this situation could be expected to create opportunities for outsourcing vendors.

The presence of a strong relationship between an organisation's IT management and its senior management team does not appear to deter organisations from adopting IS outsourcing. Exhibit III-20 shows the proportion of respondents by respondent type who perceived there to be a strong relationship between the organisation's IT management and its senior management team immediately prior to the adoption of outsourcing.

Exhibit III-20

Perceived Strength of Relationship Between IT Management and Senior Management Team



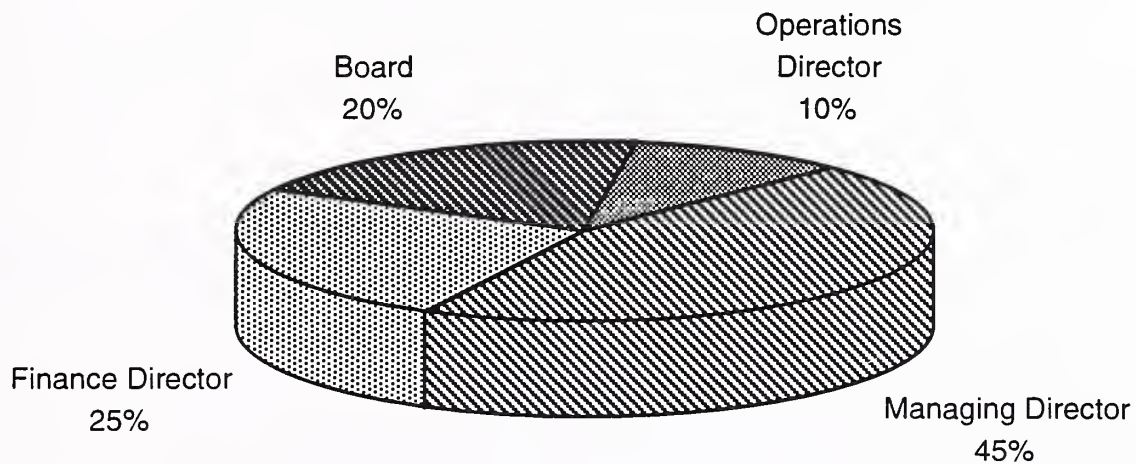
Standard error = 8%

Source: INPUT

As expected, IT managers take a more optimistic view of the strength of the relationship than other managers. However, these proportions suggest that personal relationships between IT management and senior executives are insufficient to inhibit the adoption of outsourcing.

Overall, IT directors and managers appear to have better working relationships with their CFOs than with other members of the senior management team. This may be a problem they need to overcome since IT directors are increasingly likely to report to the CEO or main board of an organisation rather than the CFO, as shown in Exhibit III-21.

Exhibit III-21

Reporting Relationship of IT Director*Standard error = 7%**Source: INPUT*

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IV

IT Directors Favour Vendors Offering Flexible Outsourcing Contracts

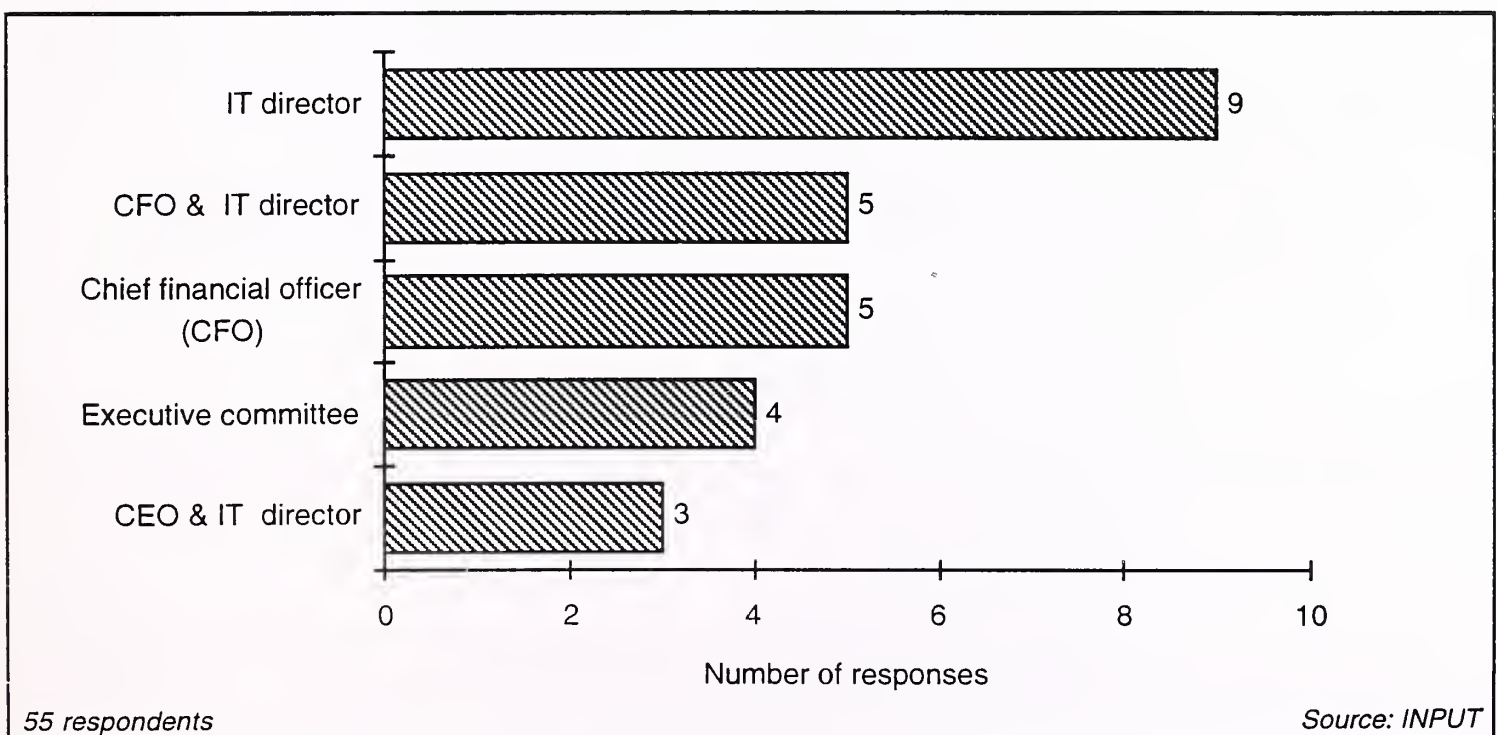
A IT Directors are the Key Parties in Vendor Selection

IT directors and managers are significantly less likely than chief financial officers to initiate IS outsourcing within their organisations. However, once the decision to adopt IS outsourcing has been taken, then IT directors become very closely involved in the selection and management of the outsourcing vendor.

Exhibit IV-1 lists the key parties involved in vendor selection.

Exhibit IV-1

Decision Makers: Vendor Selection



The IT director is typically the individual with the greatest influence during the vendor selection process. Overall, the IT director was judged to be a key influencer in vendor selection in 75% of instances, compared to 40% of instances for Chief Financial Officers, and 30% for Chief Executive Officers.

While IT directors frequently work alongside other directors during the vendor selection process, they were regarded as being solely in charge of vendor assessment in 30% of instances, a proportion approximately double that of Chief Financial Officers.

A study conducted by INPUT in the US similarly concluded that the in-house IS department dominates management of the evaluation and selection process, either through direct management of the process or leadership in many of the phases.

In particular, the IS department was identified as the leader in the following stages of the evaluation process:

- Capabilities analysis
- RFP preparation
- Selection of shortlist
- Management of bidders' conference
- Development of selection criteria
- Vendor communications
- Recommendations

On the other hand, the finance department was identified as the key area for:

- Developing financial models
- Cost analysis of proposals

Overall, the finance department plays a secondary role in the actual management of vendor selection, but has a relatively high degree of influence on the outcome by:

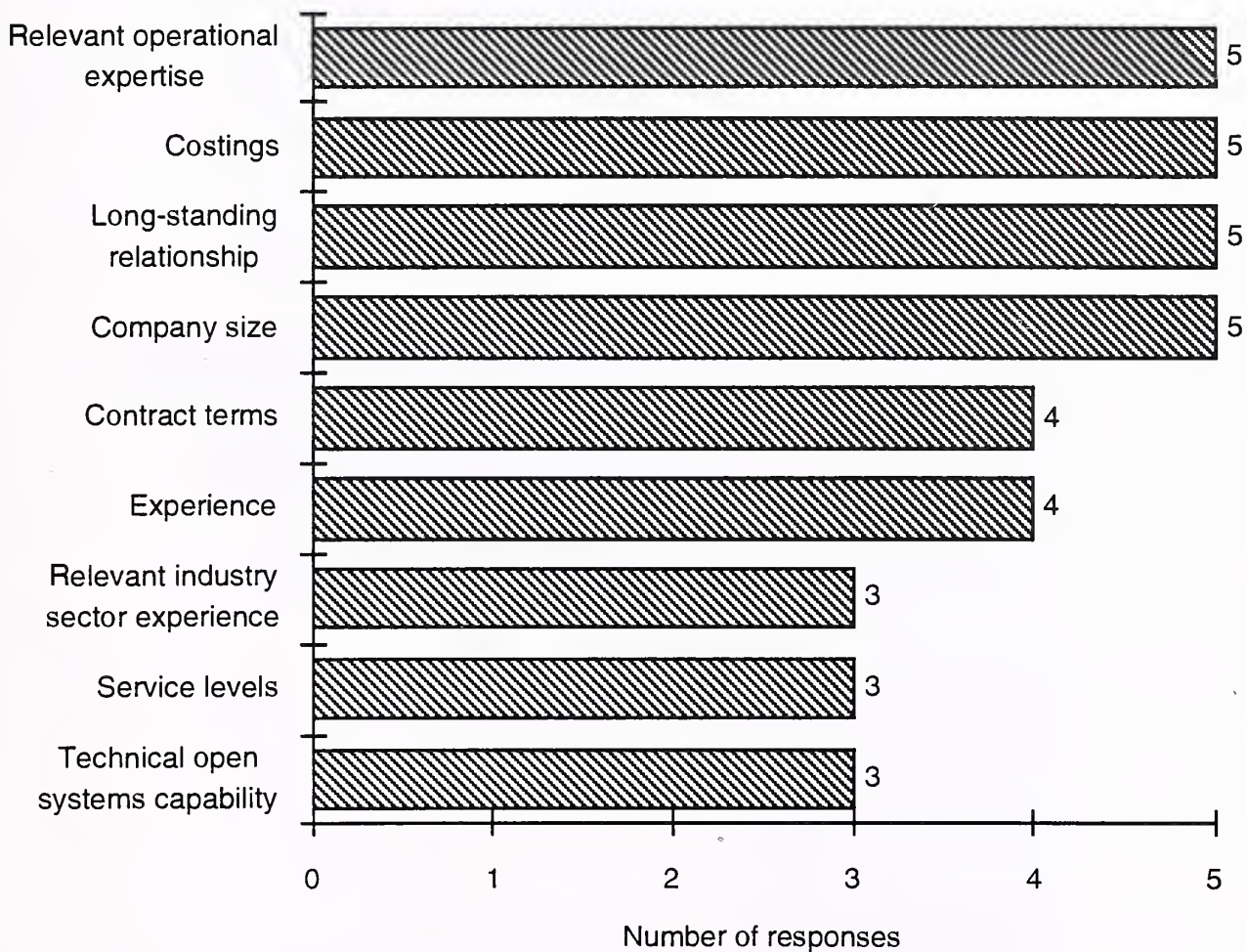
- Setting the basis for the comparison of proposals through its heavy involvement in the cost analysis activity

- Controlling the algorithmic parameters that are used to compare the financial aspects of vendor proposals through direct involvement in the development of models
- Acting as the final authority on the validity of the financial projections coming out of the process

Exhibit IV-2 lists the most frequently mentioned vendor evaluation criteria.

Exhibit IV-2

Vendor Evaluation Criteria: Europe



Sample of 55 respondents

Source: INPUT

These can be grouped into a number of categories, such as:

- The vendor's ability to provide the required services for a suitable fee, to the required service levels, and within an acceptable contractual framework

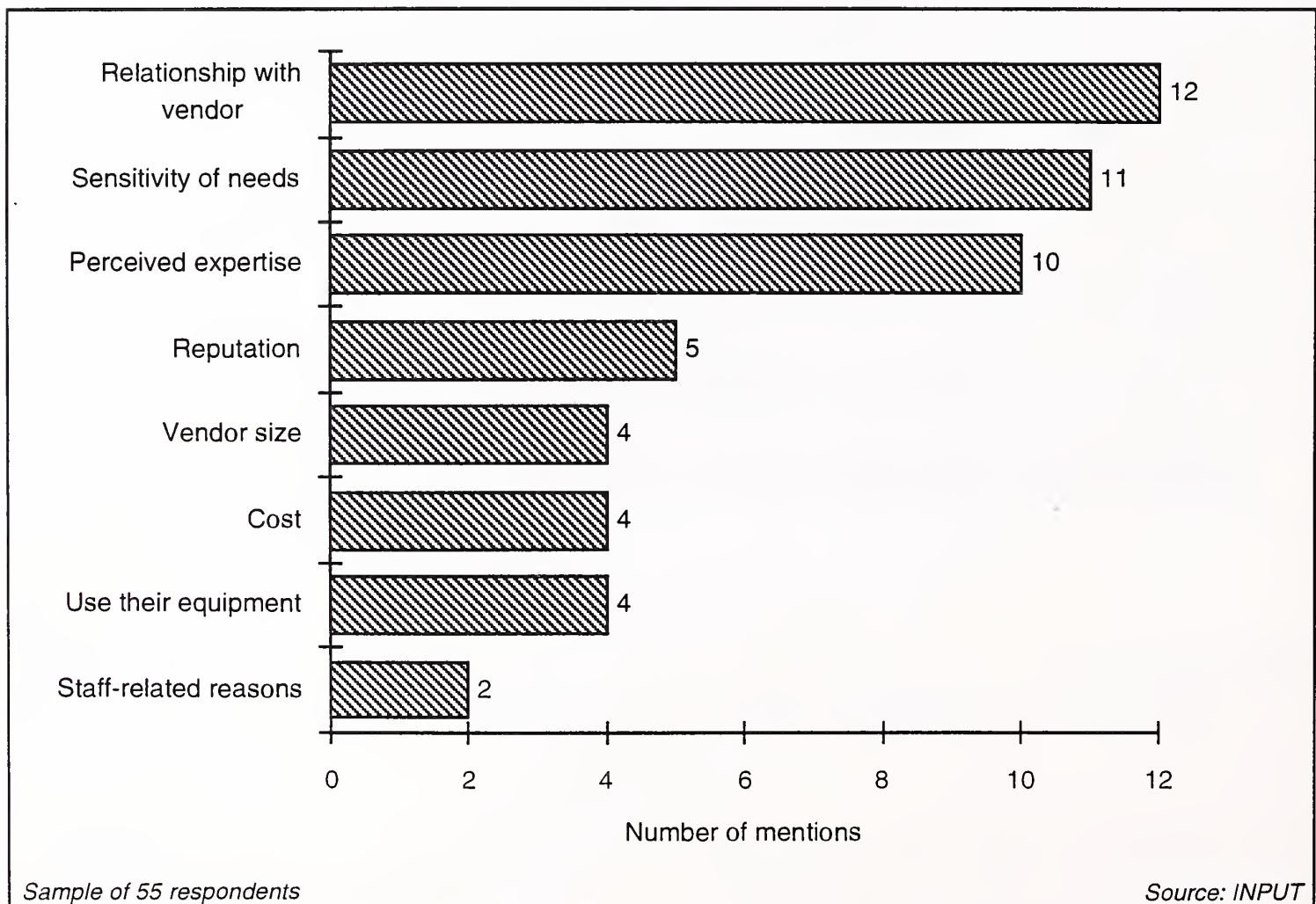
- The degree of risk involved in selecting the vendor judged in terms of the organisation's prior use of the vendor, the vendor's size and the vendor's perceived level of experience
- The vendor's capability evaluated in terms of the appropriate mix of industry-specific skills and technical skills.

B**Contract Flexibility is Important in Final Stages of Vendor Selection**

Respondents were asked both to identify (unprompted) the major reasons why they chose their favoured vendor, and also to rate the importance of each of a number of factors in influencing their choice of final vendor.

Exhibit IV-3 lists the most frequently mentioned reasons for selecting the successful vendor.

Exhibit IV-3

Reasons For Selection of Successful Vendor

It can be concluded that prior experience of an organisation gives the vendor a significant advantage in tendering for outsourcing contracts. However while a direct, long-standing relationship with the vendor had existed in the majority of cases where the vendor/client relationship was perceived to be a major determinant of success, this was not always the case. In a number of instances, recommendations, or favourable references from the parent company or fellow subsidiaries were sufficient to have a major impact on the contract award.

Where clients do not have an existing relationship with the vendor, the vendor's reputation becomes an important factor in the selection process.

Sensitivity to the client's requirements is another very important factor in achieving successful bids. Attributes that contributed strongly to vendor success included:

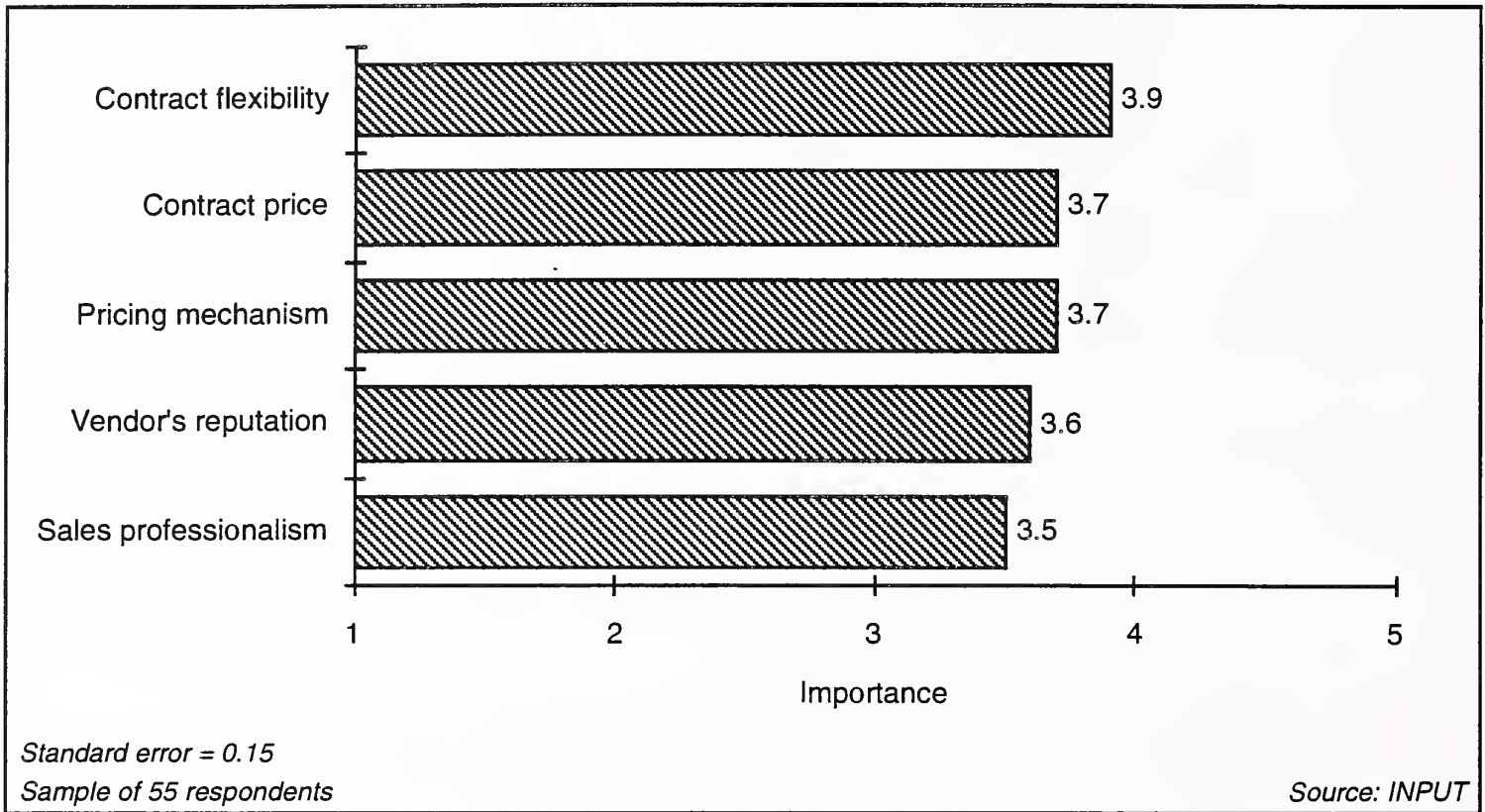
- The ability to get close to the client and share the client's vision, rather than imposing the vendor's vision on the client
- The ability to ensure that the client felt in control of their destiny
- Attention to detail
- Contract flexibility in terms of timescales and options

Third place in number of mentions was occupied by the vendor's level of expertise. This category can be broadly separated into three areas of capability:

- Most importantly, the vendor's technical skills, such as knowledge of the client's operating environment and the extent of the vendor's infrastructure management capability
- Perceived service quality including the vendor's ability to meet the desired service levels
- Industry sector-specific expertise

Respondents were also asked to rate the importance of a number of criteria in influencing their final choice of vendor. The most highly rated criteria are listed in Exhibit IV-4.

Exhibit IV-4

Criteria Influencing Final Choice of Vendor: Europe

Contract flexibility was perceived to be the most important factor of those suggested to outsourcing clients. Indeed, there are signs of a reaction in the user community against contracts that are viewed as too long or based on too rigid a framework. For example, the Royal Borough of Windsor and Maidenhead switched vendors, even after the organisation had nominated its preferred vendor, in order to reduce the contract length from five years to a more flexible three-year arrangement. Similarly, CFM won a contract with CWS because CFM was prepared to take a property lease the length of which significantly exceeded the length of the initial IS outsourcing contract.

This need for flexibility applies not only at the initial contract negotiation stage, but also during the life of the contract. For example, Heinz has recently re-negotiated the terms of its outsourcing contract with Hoskyns in mid-contract. There are indications that many users perceive a danger of outsourcing contracts locking them in to a particular architecture or framework, at a time when one of their prime requirements is to substantially enhance the flexibility of their IT support.

Exhibits IV-5 to IV-7 list the relative importance of each of the specified criteria in influencing final vendor selection within France, Germany and the UK respectively.

Exhibit IV-5

Key Criteria Influencing Final Choice of Vendor: France

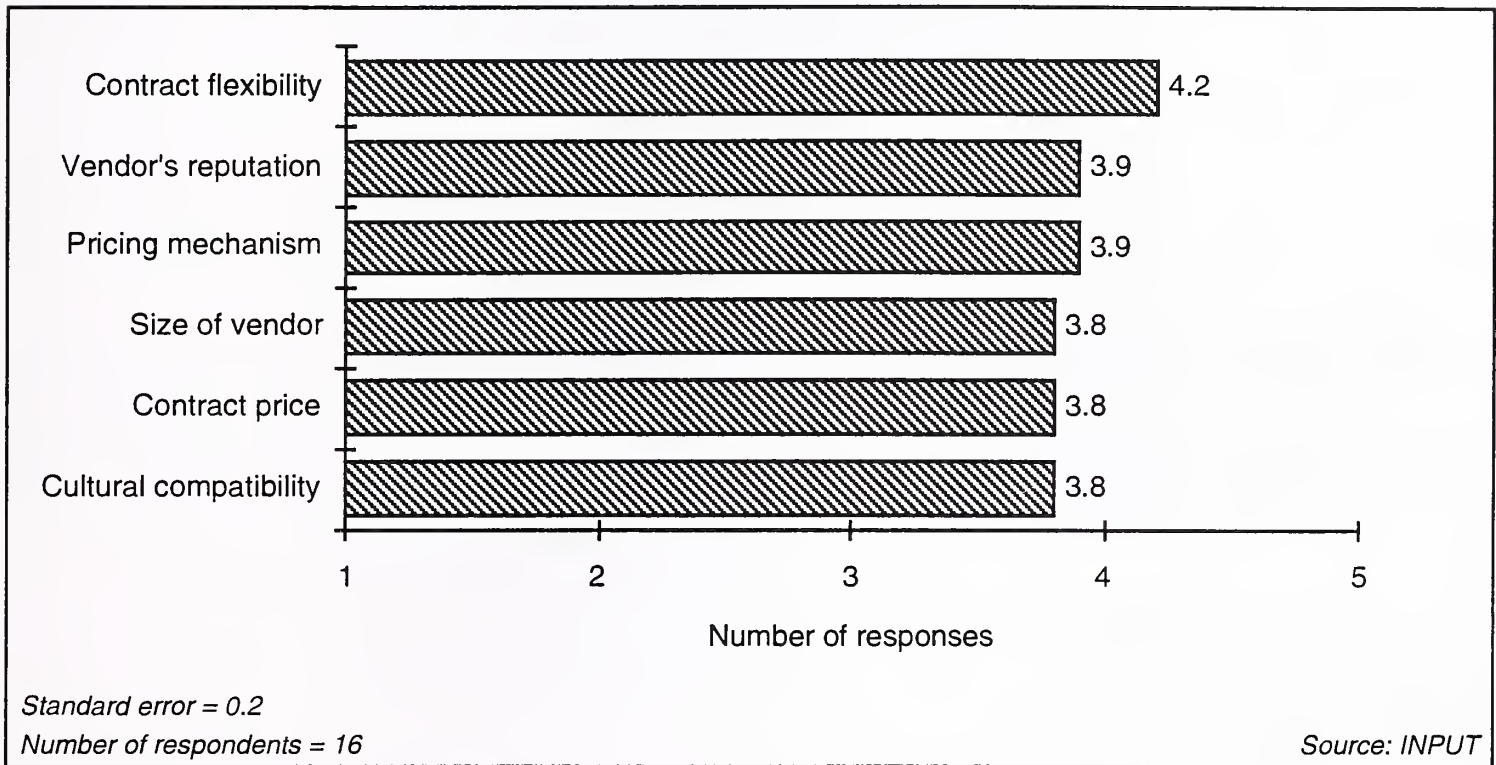


Exhibit IV-6

Key Criteria Influencing Final Choice of Vendor: Germany

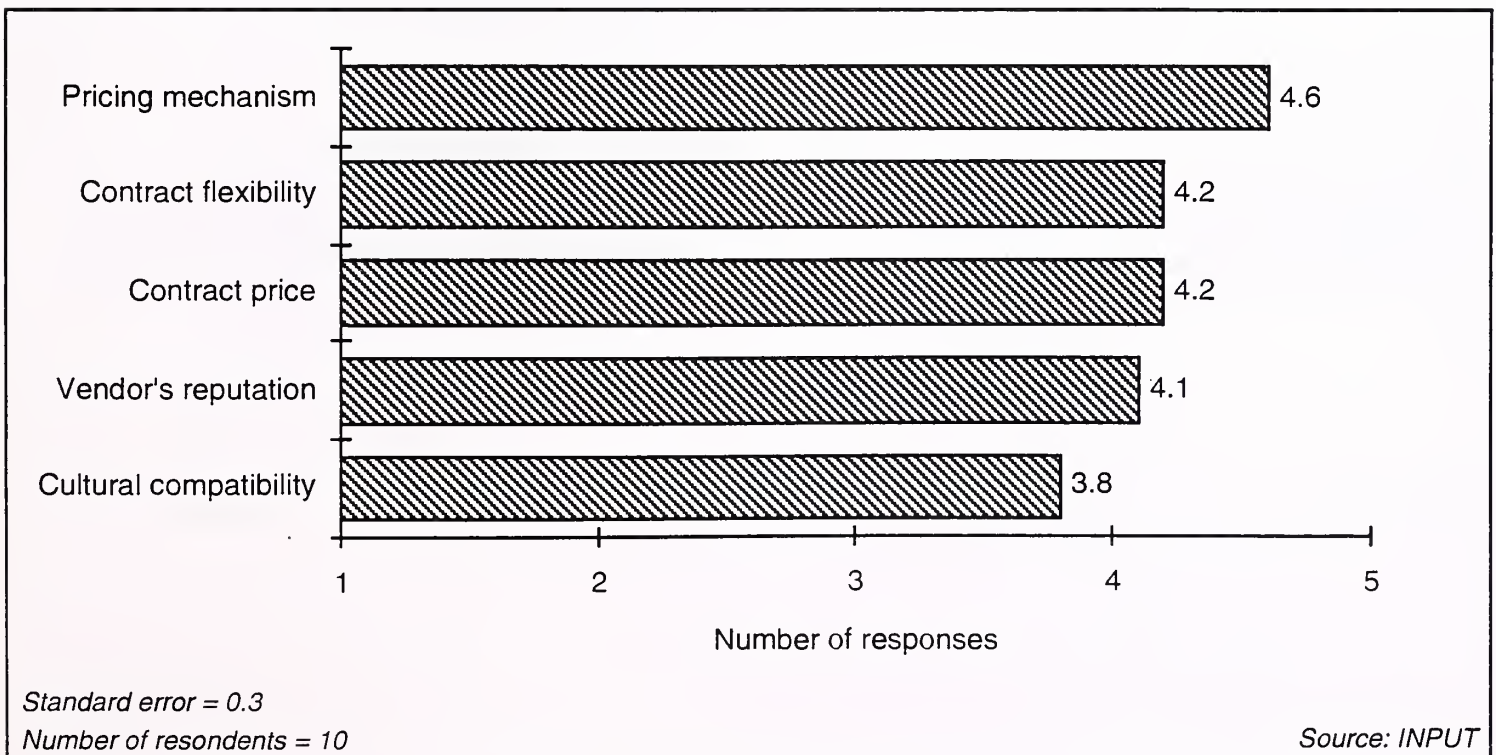
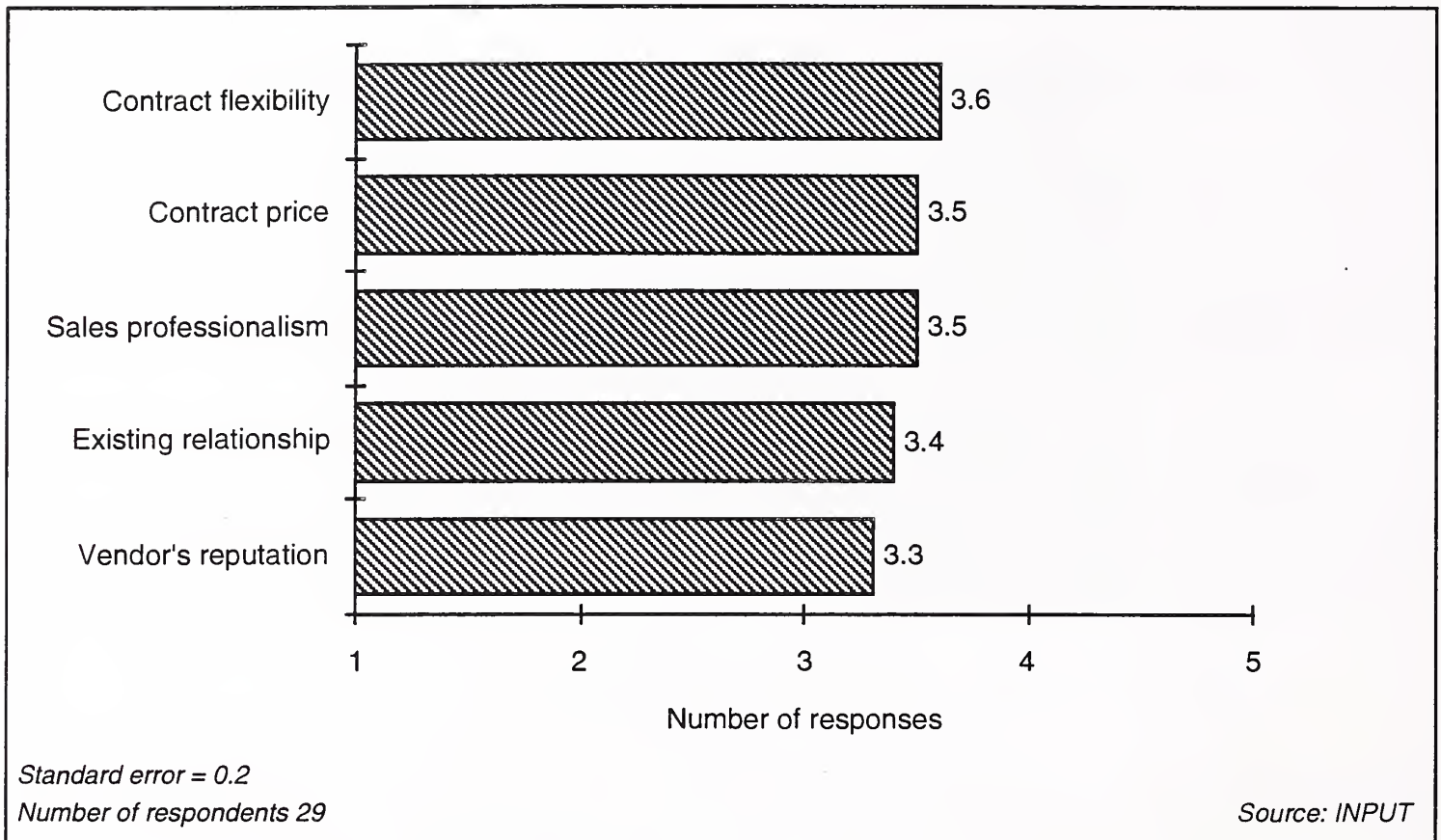


Exhibit IV-7

Key Criteria Influencing Final Choice of Vendor: UK

A breakdown of the relative importance of these selection criteria by party is shown in Exhibit IV-8.

Exhibit IV-8

Key Selection Criteria by Respondent Type

Importance	IT Directors/Managers	Chief Financial Officers	Other Senior Executives
High	Contract flexibility Contract price Pricing mechanism		Contract flexibility Contract price Vendor's reputation Pricing mechanism
Medium-High	Existing relationship Sales professionalism	Sales professionalism Contract flexibility Vendor's reputation	Cultural compatibility

Source: INPUT

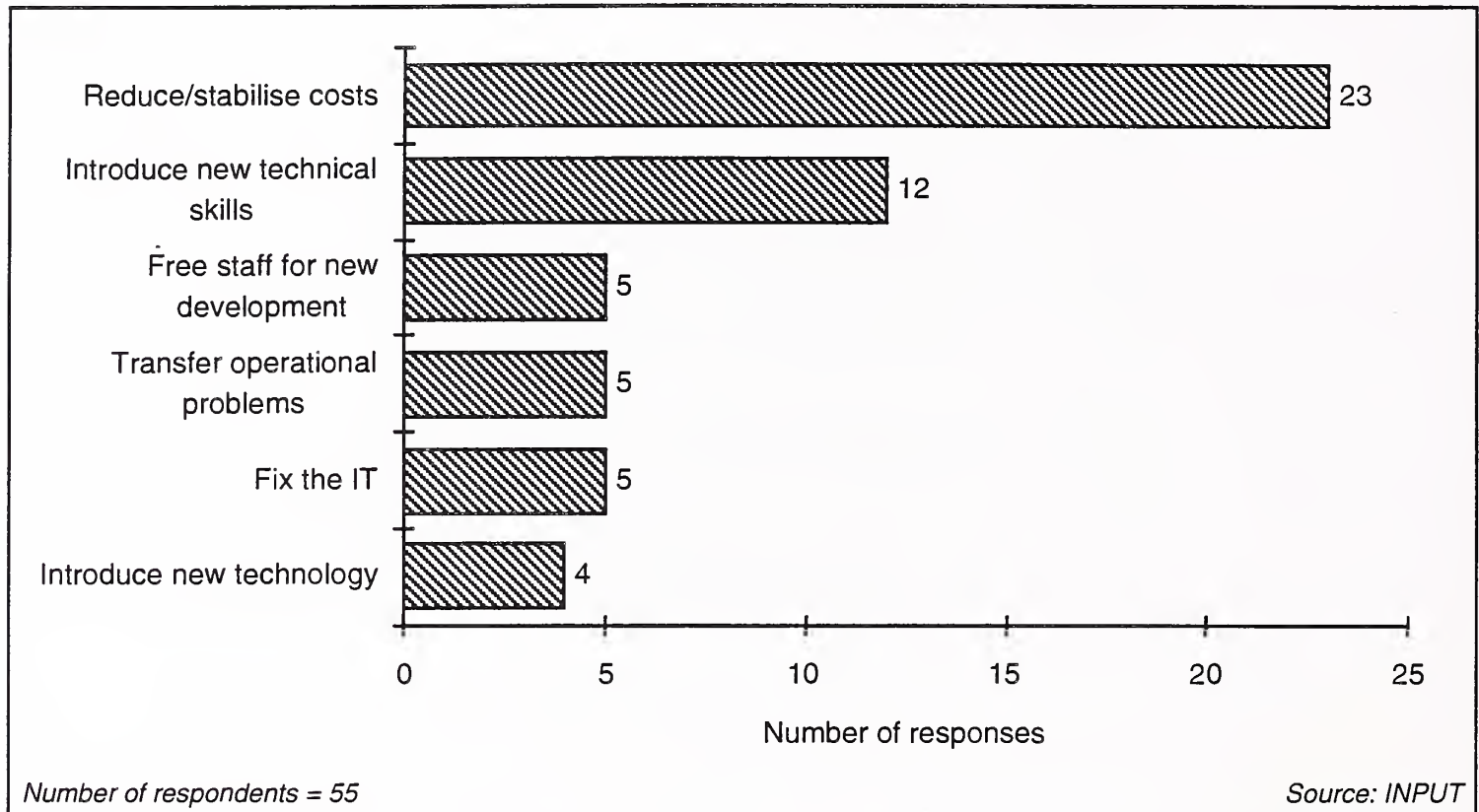
Cultural compatibility received a surprisingly low rating. This may be because cultural compatibility is best demonstrated by the vendor's existing relationship with the client and the flexibility displayed in meeting the needs of the client within the outsourcing proposal and contract.

The vendor's reputation is an important criterion for Chief Financial Officers and other senior executives, probably because these personnel tend to have limited day-to-day experience of the organisation's current information services suppliers. However, IT directors tend to be less concerned with the vendor's reputation and are more influenced by their current working relationships with vendors.

Contract price is not as important to Chief Financial Officers as contract flexibility, but remains very important to IT directors and chief executive officers. IT directors still often view cost savings as the key rationale for outsourcing as an alternative to in-house services. Similarly, chief executive officers can be expected to view comparative cost-effectiveness as a key element in benchmarking internal services to decide which should be contracted out.

Exhibit IV-9 lists the most frequently given views of the role of IS outsourcing.

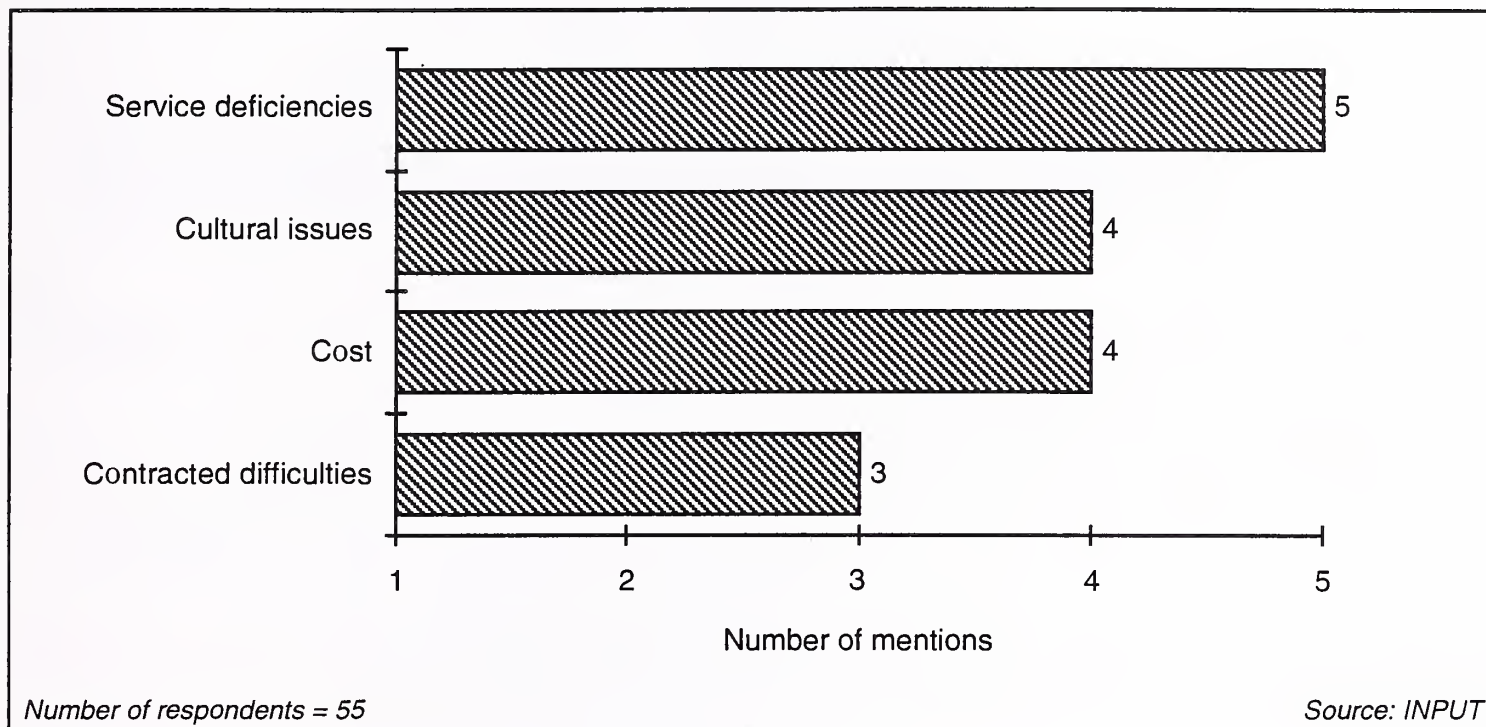
Exhibit IV-9

Perceived Role of Outsourcing: Europe

Clearly the major themes are the introduction of new technical skills and/or new technology into the organisation while minimising the impact of these changes on overall IT expenditure.

Exhibit IV-10 lists the principal reasons identified for eliminating vendors from the selection procedure.

Exhibit IV-10

Reasons for Vendor Rejection

The principal reasons given were service deficiencies or a vendor's lack of relevant areas of expertise. Specific deficiencies mentioned included:

- Lack of relevant platform expertise or other technical capability
- Lack of appropriate business acumen or application expertise
- Inadequate geographic coverage

Specific factors leading to cultural compatibility included:

- Small organisations' fear of lack of attention, or being overwhelmed, by major outsourcing vendors
- Vendors' desire to provide a greater range of services than were thought appropriate by the client
- A fear of loss of control.

In addition, a lack of flexibility has been a major factor in unsuccessful bids. Reasons cited by executives for eliminating vendors from the bidding process included excessive contract duration and potential difficulties in contract termination.

Overall, organisations remain quite well satisfied with the performance of their outsourcing vendors. Exhibit IV-11 summarises the degree of satisfaction of the various parties primarily involved in the initiation and purchase of IS outsourcing.

Exhibit IV-11

Level of Satisfaction with IS Outsourcing

Respondent Type	Importance of IT	Outsourcing Satisfaction Rating
CFO	4.3	3.9
Other senior executives	3.7	3.7
IT directors/managers	4.3	3.7
All	4.1	3.7

Source: INPUT



User Questionnaire

A

Initiation

- 1(a). Who, within your organisation, was the major influence in the decision to evaluate or adopt IT outsourcing?

Job Title _____

- 1(b). How influential were each of the following in promoting the use or evaluation of IT outsourcing? (Please rate on a scale of 1-5 where 1 = no impact and 5 = a major influence)

Managing Director/Chief Executive Officer _____

Financial Director/Chief Financial Officer _____

Other Director (please specify) _____ Job title _____

External consultancy _____

Outsourcing vendor _____

- 2(a). What circumstances led to the decision to evaluate or use IT outsourcing?

- 2(b). How important were each of the following factors? (Please rate on a scale of 1-5 where 1 = not at all important and 5 = extremely important)

Overall financial circumstances _____

Desire to reduce IT expenditure _____

Desire to reduce IT headcount _____

Desire to remove equipment from balance sheet _____

Desire to change IT architecture/infrastructure _____

Desire to apply up-to-date technology to the business _____

Corporate restructuring or downsizing _____

Decentralisation/creation of autonomous business units _____

Desire to improve focus of IT department _____

Internal IT skill or resource shortfalls _____

3(a). Did any specific event(s) trigger the decision to adopt/evaluate IT outsourcing?

Yes/No

If so, what were they?

3(b). To what extent did your decision to adopt/evaluate outsourcing coincide with any of the following? (Please rate on a scale of 1-5 where 1 = not at all and 5 = very significantly)

Appointment of key member of management team _____ Title _____

Worsening of company's financial circumstances _____

Major restructuring exercise _____

Solicitation by outsourcing vendor _____

Loss of key IT manager(s) _____

Need for major IT systems redevelopment _____

Evaluation of core business focus throughout business _____

4(a). How efficient was your in-house IT department perceived to be at this time?
(Please rate on a scale of 1-5 where 1 = not at all efficient and 5 = very efficient)

4(b). How effective was your in-house IT department perceived to be at this time?
(Please rate on a scale of 1-5 where 1 = not at all effective and 5 = very effective)

- 4(c). To whom did your senior IT manager or Director report immediately prior to the decision to adopt IT outsourcing?

Job title _____

- 4(d). Was the IT department organised on a centralised or decentralised basis?

Centralised _____ Decentralised _____

- 4(e). How strong was the relationship between your IT manager and the senior management team at this time? (Please rate on a scale of 1-5 where 1 = weak and 5 = very strong)

- 5(a). Which of the following aspects of your IT function did you decide to outsource?
The operation and management of "old" systems while new ones are developed

Yes/No If so, why?

The support and maintenance of in-house developed systems

Yes/No If so, why?

The operation and management of computer equipment or data centres

Yes/No If so, why?

The support of the personal computer infrastructure including LANs

Yes/No If so, why?

The operation and management of wide area and other telecommunication networks

Yes/No If so, why?

Other (please specify _____)

5(b). Why did you decide not to outsource the remainder of your IT function?

6(a). What role did you expect IT outsourcing to play within your organisation?

6(b). How has this expectation subsequently changed?

B

Vendor Selection Criteria

7(a). What were the principal stages of your vendor selection process?

7(b). What were the principal vendor evaluation criteria at each stage?

7(c) Who was in charge of vendor evaluation at each stage? For example, IT manager, Finance Director, etc.

Stage	Evaluation Criteria	Controlled by

8. Why was each of the unsuccessful vendors ruled out and at which stage of the evaluation process?

Stage	Evaluation Criteria	Controlled by

9. Why was the successful vendor(s) chosen?

Vendor	Reasons for Success

10. Overall, how important was each of the following factors in influencing your final choice of vendor? (Please rate on a scale of 1-5 where 1 = irrelevant and 5 = very influential)

Existing relationship with vendor	_____
Vendor's reputation in marketplace	_____
Appropriate size of vendor	_____
Professionalism of sales team	_____
Contract pricing mechanism	_____
Flexibility of contract	_____
Contract price over life of contract	_____
Cultural compatibility with vendor	_____

11. How important do you perceive IT to be in the future development of your business? (Please rate on a scale of 1-5 where 1 = minor contribution only and 5 = critical to the future success)

12. What is your current overall level of satisfaction with your outsourcing vendor's performance? (Please rate on a scale of 1-5 where 1 = very dissatisfied and 5 = very satisfied)

13. When did your outsourcing contract commence? _____
14. What is the duration of your outsourcing contract? _____
15. What is the approximate lifetime or annual value of this contract? (Please state period covered and currency used) _____

Thank you for your assistance

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